Ontario

Legislative Assembly

1975

REPORT OF THE SELECT COMMITTEE ON COMPANY LAW ON LOAN AND TRUST CORPORATIONS

TABLED IN THE LEGISLATIVE ASSEMBLY BY
WILLIAM HODGSON, M.P.P.,
CHAIRMAN

5th SESSION, 29th LEGISLATURE, 24 ELIZABETH II

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PROVINCE OF ONTARIO
LEGISLATIVE ASSEMBLY
SELECT COMMITTEE ON COMPANY LAW
REPORT
ON
LOAN AND TRUST CORPORATIONS

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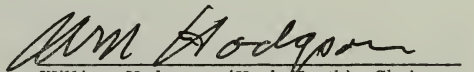
LETTER OF SUBMISSION

TO: The Honourable Russell D. Rowe,
Speaker of the Legislative Assembly of the
Province of Ontario

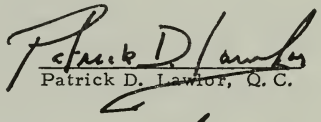
Sir:

We, the undersigned members of the Committee appointed by the Legislative Assembly of the Province of Ontario on December 17, 1971 to enquire into and review, inter alia, the law affecting the corporations of this Province and to enquire into and report upon certain specialized types of corporations, in particular, loan and trust companies, together with the legislation of other jurisdictions relating to the same, have now the honour to submit the attached Report on these subjects.



William Hodgson, (York North), Chairman

J. Albert Belanger



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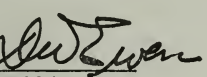

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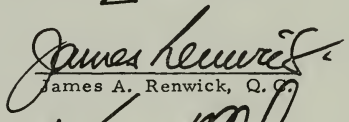

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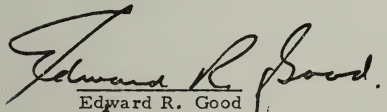

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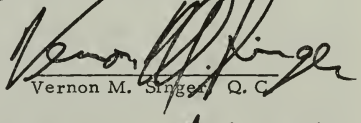

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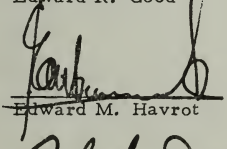

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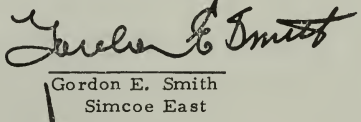

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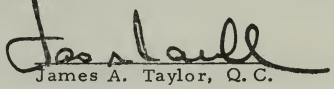
Simcoe East

Robert M. Johnston



James A. Taylor, Q. C.
Prince Edward-Lennox

INTRODUCTION

The Select Committee on Company Law was reconstituted on December 17, 1971. Under its revised terms of reference, the Committee was appointed:

> "to continue the enquiry and review of the law affecting the Corporations in this Province as reported on by the Select Committee of this House appointed on June 22, 1965, and re-appointed on July 8, 1966, and on July 23, 1968, and in particular, to enquire into and review the law relating to mergers or amalgamations, the rights of dissenting shareholders in the event of various fundamental corporate changes, the purpose, function and scope of the annual return, the law relating to the protection of the creditor, and the dissolution of the ordinary commercial corporation in Ontario.
> And further, to enquire into and report upon such specialized types of corporations as insurance companies, loan and trust companies, corporations without share capital, finance and acceptance companies, and extra-provincial companies, together with the legislation of other jurisdictions relating to the same matters."

When appointed, the Committee was composed of eleven members—Mr. Meen (Chairman), Messrs. Clement, Good, Hodgson (York North), Johnston, Lawlor, Reilly, Renwick, Mrs. Scrivener, Singer and Smith (Simcoe East). On June 30, 1972, Mr. Meen resigned as Chairman of the Committee upon his being appointed a Parliamentary Assistant, although he continued to be a member of the Committee. Mr. Clement thereupon became Chairman of the Committee. On December 15, 1972, Mr. Clement resigned as the Chairman and as a member of the Committee upon his being appointed the Minister of Consumer and Commercial Relations. Mr. Hodgson thereupon became Chairman of the Committee and Mr. Allan was appointed to the Committee to fill the vacancy created by Mr. Clement's resignation. On May 3, 1973, Mr. Allan retired from the Committee and Mr. Belanger was appointed to fill the vacancy that had been created. In June, 1974, Messrs. Meen and Reilly and Mrs. Scrivener resigned in view of Mr. Meen's appointment as Minister of Revenue and the appointment of Mr. Reilly and Mrs. Scrivener as Parliamentary Assistants and Messrs. Ewen, Havrot and Taylor (Prince Edward-Lennox) were appointed to replace them.

The new topic selected during 1973 for consideration by the Committee was the law relating to loan and trust companies. This topic, so

far as can be established, has never been the subject of a study by a Select Committee of the Legislature. The principal statute reviewed was The Loan and Trust Corporations Act which provides for the incorporation and registration of loan and trust companies in Ontario. Due to the fact that the dissolution of corporations is a specialized topic within the Committee's terms of reference and that mergers or amalgamations of corporations have already been the subject of a report by the Committee, these matters are not discussed in this report.

Submissions were invited from interested persons including all registered corporations. The Committee held 45 meetings between January 1, 1974 and January 23, 1975. We are indebted to many people who devoted their time freely and helped us immeasurably.

In February, 1974, the Committee spent two days in New York City in order to study the loan and trust institutions of that jurisdiction and to hold discussions with those specialists who had acquired practical expertise in this field. The Committee had meetings with the following: Mr. D. R. McCallum, Senior Vice President of the Bank of Montreal Trust Company; Mr. Boris S. Berkovitch, Senior Vice President of the Morgan Guaranty Trust Company of New York; Messrs. Thomas A. Melfe and William D. Doino, Vice Presidents of the United States Trust Company of New York; Messrs. Robert J. Crowley, Assistant Vice President and Thomas Adams, Senior Trust Examiner, of the Federal Reserve Bank of New York; Roy Haberkern, Esq., of Milbank, Tweed, Hadley and McCloy, attorneys-at-law representing the Chase Manhattan Bank; and Messrs. James Bolster, Deputy Superintendent, and Victor V. Pesci, Examiner, of the Banking Commission of the State of New York.

In September, 1974, the Committee spent ten days in London, England, for the purpose of learning from those in that country who had specialized in the law and practice applicable to trust companies and similar institutions. The Committee had meetings with the following: Sir Hilary Scott and Mr. H. C. Rumbelow of Slaughter and May, solicitors; Mr. H. D. Osborne, a director of The Law Debenture Corporation, Limited; Mr. Geoffrey Williams, a director of J. Henry Schroder Wagg & Co. Limited and of Schroder Executor and Trust Company; Michael M. Wheeler, Q.C., a company and chancery barrister; Mr. R. C. M. Cooper, Under-Secretary of the Companies Division of the Department of Trade; Mr. S. G. Linstead of the Department of Trade; Mr. H. H. W. Duffy, the Assistant Public Trustee: Mrs. S. V. Glyn-Owen, a barrister associated with the Lord Chancellor's Office; Mr. M. S. Morris, the Under-Secretary of the Insurance Division of the Department of Trade; Mr. Keith Brading, Chief Registrar of Friendly Societies and Building Societies; Mr. N. E. Griggs, the Secretary General and Graham Pitt, Esq.,

the Deputy Secretary General, of The Building Societies Association; Mr. A. Mason, the General Manager of The Provincial Building Society; and Mr. G. E. Bainbridge, C.A., of Robson, Rhodes and Co., who are chartered accountants and auditors of The Provincial Building Society.

The Committee wish to express their thanks to Mr. Lawrence Robson, C.A., of Robson, Rhodes and Co. and to The Lady Robson for their most generous hospitality.

The Trust Companies Association of Canada has been most helpful and we thank Messrs. E. F. K. Nelson, Eric Brown, Q.C., R. H. Dunlop, A. C. C. Hedge, William Potter, R. R. Merrifield, Q.C., J. E. Donahoe, B. B. Upshall, David E. Allin, James Sayers and C. T. Manning, Q.C., all of whom devoted most generously of their time and experience to assist the Committee. Others from the loan and trust community to whom the Committee is grateful include Messrs. W. Kucherepera, P. L. E. McAvoy, E. D. L. Miller, J. Clarke, A. P. Smibert, A. Fricker, D. Bosworth, and D. M. McClelland.

The Committee is also grateful to Mr. Richard Humphrys, Federal Registrar of Loan and Trust Companies, who met with the Committee and made a contribution from his broad experience.

The work of the Committee was greatly assisted by the representatives of the Ontario Ministry of Consumer and Commercial Relations and particularly the Registrar of Loan and Trust Corporations, Mr. Gordon E. Grundy, F.C.A., who was the Registrar throughout the period of the Committee's sittings. He gave unstintingly of his time and of his immense experience and made a vital contribution to the work of the Committee. The Committee wishes, with deepest regret, to record his passing on March 28, 1975 and to pay tribute to his dedication to the work of his office. The Ministry was also ably represented before the Committee by Murray A. Thompson, Esq., who is now the Registrar and was formerly the Assistant Registrar, Mr. Robert Brewerton, C.A., the Chief Examiner and Mr. Harry R. Terhune, the Assistant Chief Examiner, all of whom gave generously of their time and knowledge, and greatly assisted the Committee in the carrying out of its investigations.

This work could not have been accomplished so effectively and efficiently without the able guidance of our Counsel, David M. Harley, Q.C., of Borden & Elliot, and of our Associate Counsel, R. George Ness, Q.C., of Ness & Winters, and the capable assistance of our Research Director, Miss Elizabeth Burt. The Committee also benefited by the advice of our consultant on accounting matters, Mr. Peter E. Held, C.A., of Dunwoody & Co., Chartered Accountants, and by his review of Chapters 18 and 19 of the report.

Our very special gratitude goes to Mrs. Frances I. Nokes, who has been the Clerk of the Committee since it was first created. She has been ably assisted by our secretary Miss Sandy Davidson.

The reader is referred to paragraphs 2.01, 2.02, 2.03 and 2.05 of the report which contain definitions of the phrases "the Act", "the BCA", "the Federal Acts", "Ontario corporations", "federal companies", and "extra-provincial companies". These expressions are frequently used throughout the report as defined terms.

CHAPTER 1

History

Loan Corporations

1.01 Among the needs of the early settlers in what is now the Province of Ontario were institutions to provide capital for the growing colony. The first efforts to accumulate and provide capital in the early 19th century included the granting of extended terms of credit by individual merchants, faltering attempts to establish private banks, the founding of chartered banks, the use of local lawyers as mortgage brokers, and to some degree a reliance on loan companies operating from Great Britain. In seeking to fulfil their capital requirements, the colonists naturally drew upon the experience that they had accumulated in Great Britain prior to their departure. One of the British institutions which they adopted was the building society.

1.02 British building societies were developed in the latter part of the 18th century and in the early 19th century. The societies were composed of small groups of people of modest means who were inexperienced in matters of capital and investment; they were established for the specific and limited purpose of accumulating capital for the acquisition of housing for the members as promptly as possible; and they were operated on a co-operative basis by the members themselves. The societies were, at least initially, intended to fulfil their members' needs and having achieved their purpose, to be wound up. Hence their early designation as "terminating building societies".

1.03 In 1846 the Building Societies Act[1] was passed providing for the establishment of building societies in Canada West (now Ontario). It provided for the incorporation of building societies with at least 20 members for the purpose of raising money by way of the sale of shares of the society to its members for amounts not exceeding £100 per share, such shares to be paid for in monthly instalments of not more than 20 shillings each. The funds so raised were to be used for the sole purpose of enabling members to receive amounts up to the value of their shares in the society in order to build or buy a house or other real property. Money loaned to a member was to be secured by mortgage. Finally, due provision was made for the manner in which the society was to be organized and operated.

1.04 Prompt advantage was taken of the new legislation. The Port Sarnia Syndicate, an unincorporated society, was registered in 1847 as The Port Sarnia Building Society, to which the present Lambton Loan and

Investment Company is the successor[2]. By 1855, 18 building societies had been incorporated in the County of York alone. This immediate popularity of building societies attests clearly to the needs of the time.

1.05 A typical early building society conducted its business in approximately the following manner. On incorporation the society would have 20 members. Each member would subscribe for a share at a price of £100 payable in monthly instalments of 20 shillings each until the share was fully paid, allowance being made for such part of the society's earnings as might be credited to that share. When the fund of cash on hand became large enough to justify the making of a loan, the members met together and an auction was held. The loan was auctioned to the member who was willing to pay the largest bonus, over and above the fixed interest rate, in return for receiving the loan. Each loan was limited to the amount of the borrowing member's share subscription and the advancing of the loan was subject to the giving of security by way of a mortgage upon the house being acquired. The earlier loan recipients generally paid the highest bonuses and received their house financing loans first, while those who delayed their house purchase the longest paid the least, because of the diminishing demand for loan funds amongst the membership. When loans had been obtained by all the members, it was the intent that the society would be wound up and its assets, including profits from interest and bonuses, would be distributed amongst the membership. The out-of-pocket expenses of managing the society were met from an entrance fee and from nominal monthly dues that were levied upon the membership. The actual management was in the hands of the members themselves.

1.06 While the original intent of the building society was that it should be terminated when its purpose was fulfilled, in practice the societies tended to add new members as the original members' needs were met. The early societies were expected to wind up their affairs in about 14 years but plans were soon underway for the re-constitution of the "terminating societies" as "permanent societies". The first evolution of such a society occurred in 1855 on the amalgamation of the Farmers' and Mechanics' Building Society with the Toronto Building Society. Together they formed the Canada Permanent Building and Savings Society, to which the present-day Canada Permanent Mortgage Corporation is the successor[3]. Other societies soon followed suit, and, with the passing of the Building Societies Act of 1859, statutory recognition of the permanent societies was granted[4]. Thus within a short period of time the simple artisans' societies had taken a major step toward becoming professional, permanent financial institutions. After an initial flourishing, however, the societies diminished in number. Enthusiasm was sometimes unaccom-

panied by experience, and so bad judgment took its toll. The small size of most societies made full-time management impossible and denied them the economies and the managerial skills that would have enhanced their success. Gradually the desirability of consolidation and permanence among the societies became obvious and the remaining societies became larger as they became permanent.

1.07 In 1875 Ontario enacted the Permanent Building Societies Act[5]. It permitted societies for the first time to lend money to non-members, to purchase mortgages, and to invest in federal, provincial and municipal securities. It also permitted societies to borrow by issuing debentures. Further, it provided the first regulatory legislation, including the granting of power to the Provincial Treasurer to stay the conduct of a society's business in the event of improper management. In 1891 Ontario enacted its first loan company legislation.[6] The new Act, called "An Act respecting Loan Companies", was expressed to apply to "all companies which may hereafter be incorporated for the purpose of lending money on real estate or other securities hereafter mentioned". It did not apply to building societies, except for some express references to them. The 1891 Act was soon followed by The Loan Corporations Act of 1897 which consolidated the law relating to loan companies and building societies and repealed the outstanding legislation concerning these companies and societies.[7] The evolution of the loan corporation was complete, and the building society ceased to be a part of the financial system of Ontario.

1.08 The importance of the loan corporation as a Canadian financial institution reached its zenith in the 1890's. By that time loan corporations had succeeded in acquiring control of about 24 per cent of all assets controlled by financial intermediaries in Canada. Thereafter this share of business dwindled until, by 1944, it had dropped to about two per cent; since then it has shown some growth although total assets remain small relative to those of other financial institutions.[8] The early success of loan corporations had been based largely upon their ability to market their debentures in Great Britain, and they stressed this source of capital to the detriment of the development of sources of funds within Canada itself. Then in the 1890's interest rates on Canadian loans dropped in relation to British interest rates so that the companies' debentures could no longer enjoy a competitive advantage in the British market. This setback was followed by the difficulties that were inherent in the borrowing of British funds during and after the First World War. By the time the loan corporations began to turn their focus upon Canadian depositors and debenture holders as sources of funds, other financial institutions were already actively competing for funds in the Canadian market; hence the drop in the loan corporations' relative

importance amongst the financial institutions. It is important to add, nowever, that their 1973 share of the assets controlled by Canadian financial intermediaries nevertheless represented close to six billion dollars. This compares with the approximately ten and one-half billion dollars of assets held by the trust companies (excluding their estate, trust and agency funds).[9] About 80 per cent of these funds have traditionally been invested in residential mortgages.

Trust Companies

1.09 The traditional view of English law has been that a trust is a confidence reposed in a person with respect to property of which he has possession to the intent that he will hold the property for the benefit of another; that a trustee has a duty to act with fidelity and reasonable diligence in all his dealings with the trust property and with the beneficiary of the trust; that a trustee ought not to benefit from his trusteeship; and that the courts must exercise full jurisdiction over the conduct and the conscience of the trustee.[10] Since a corporation has neither a conscience nor a responsibility in the sense that an individual has, the view of the early English law was that only an individual could act as trustee. Against this background, it is therefore not surprising that the trust company was not generally accepted in Ontario until the 1880's.

1.10 Prior to the advent of the trust company, trusteeship functions were carried out by individuals such as lawyers, accountants, local agents and others having varying degrees of expertise. The substantial increase in commerce and wealth that had occurred within Ontario by the 1870's had caused a corresponding increase in both the volume and the complexity of trust services that were required. To the need for professional executors was added the need for long-term estate managers, corporate bond trustees, transfer agents and registrars, receivers and liquidators and all the similar services that are incidental to the conduct of commercial affairs. Growing experience pointed to certain advantages of the well-organized corporation: its perpetual existence, its capacity for combining diversified skills, and its adaptability to financing requirements.

1.11 Experiments with corporate trustees had begun in the State of New York. There, despite the same English legal traditions that Ontario shared, the legislature had granted trust powers to an insurance company in 1822. Later, in 1853, the United States Trust Company of New York was incorporated with the power to carry out trusteeship functions exclusively.[11]

1.12 Isolated efforts had been made in this province as early as 1853 to obtain the incorporation of trust companies but all proposals were rejected until 1872 when The Toronto General Trusts Company was

incorporated by special act of the Ontario Legislature.[12] It did not begin operations however until 1882.

1.13 In 1882 the Ontario Legislature amended[13] The Joint Stock Companies' Letters Patent Act to make specific provision for the incorporation of trust companies. The evolution of the trust company concept can be seen in the succeeding legislation. In 1891 trust companies were authorized to act alone as trustees in High Court matters.[14] The Ontario Trust Companies Act of 1897[15] was the first effort to establish a comprehensive trust company statute. It provided for incorporation by letters patent subject to Cabinet discretion. Applicants were required to establish that their fitness to discharge trust duties was such as to command the confidence of the public, and also that the public convenience and advantage would be promoted by the granting of incorporation. In addition to Cabinet approval, a reference was to be directed to the High Court to determine whether there was any necessity for the incorporation of the proposed trust company and whether it would serve the public convenience. The paid-up capital stock had to be $100,000 before letters patent could be issued. No provision was made to accept deposits and the issue of debentures was forbidden. In order to provide a regulatory system, the High Court was authorized to cause the affairs of trust companies to be investigated. This first general statute illustrates the original emphasis upon the role of the trust company as a provider of services rather than as a financial intermediary. It also illustrates that there was legislative concern from the inception of trust company legislation with the same topics that are of concern today: the discretion to be exercised upon incorporation, the need for adequate capitalization in order to provide protection to clients, the concern about borrowing and investment powers, and the manner of regulation of the industry.

1.14 In 1912 The Ontario Trust Companies Act and The Loan Corporations Act were both repealed and were replaced by The Loan and Trust Corporations Act.[16] The combining of the two statutes recognized the fact that the trust companies were beginning to broaden their activities beyond the provision of the services of traditional trustees and, like the loan corporations, had entered the field of financial intermediation. In providing for the exercise of this function, the 1912 statute established permanently the conceptual basis for the trust companies' role in our financial system. They were prohibited from borrowing money by taking deposits or issuing debentures; on the other hand, they were authorized to accept money as trustees for investment, and in 1921 they were also permitted by an amendment to the 1912 Act to accept deposits for investment as trust funds.[17] This authority was extended to permit them to guarantee repayment of the moneys so received,

to guarantee payment of a fixed rate of interest thereon, and to retain any interest earned by them above that agreed rate. With this extension of the concept of trusteeship the way was opened for the trust companies to pursue their function as financial intermediaries; a function they have pursued to a significant and substantial extent as will be discussed further in paragraph 1.16 and Chapter 7.

1.15 It has been important for the companies to retain the character of trustees in their financial intermediary activities for at least two reasons. First, the notion of fidelity and diligence that was at the core of traditional legal concepts of the trustee appears to have been clearly associated in the public mind with trust companies. This has given the companies a prestige that they have prized from their very beginnings and has also set a high standard of conduct for the companies to observe. Second, the characterization of the companies' financial activities as a type of trusteeship service rather than as a banking business has ensured their continued regulation by the provinces. Should they be deemed to be carrying on business as banks, they would also be subject to federal jurisdiction, since "banking" is a field of legislation reserved to the federal government under the British North America Act. It has been important for the trust companies to be able to grow and flourish under the jurisdiction and encouragement of the provinces because of the very considerable competitive advantages enjoyed by the much larger chartered banks within the Canadian banking system. It appeared to the Committee that provincial legislatures, in legislating with respect to trust companies, have proceeded on the basis of a firm conviction that trust companies, many of which are provincially incorporated institutions, merit the encouragement and special interest of the provinces concerned.

1.16 The trust companies' trusteeship services have continued to expand since the end of the 19th century. This trend was accelerated as Canadian industry increasingly adopted public financing as a source of funds, since public financing carried with it an ever increasing need for the services of corporate trustees for bond issues, for stock transfer agencies, and the like. In more recent years, the traditional concept of the trustee as a supplier of services has seen even greater extension with the establishment of specialized facilities such as real estate departments. Even more striking, however, has been the increase in financial intermediation activities. By 1910 the total assets in company funds and guaranteed investment money held by Canadian trust companies constituted about two per cent of the total assets controlled by all financial intermediaries. By 1970 this ratio had climbed to almost seven per cent. In absolute terms the increase over the period was from ten million dollars to approximately ten billion dollars.[18] Today the industry in Ontario is comprised of 38 registered trust companies.

1.17 As company funds and guaranteed funds increased, the trust companies were faced with a problem as to choice of investments. Funds accepted on a demand or short term basis have to some degree been matched by short term investment in an approved list of highly secure investments that has been developed within the provisions of the Act. Funds received on a longer term basis have been matched where possible by corresponding investment in relatively more fixed investments, predominantly in the residential mortgage field. Thus by 1970, mortgage loans accounted for 58 per cent of total assets and the trust companies had become the principal source of residential mortgage funds among private lenders.[19] In recent years the companies have entered other investment fields such as personal loans. The traditional trustee concept has proven sufficiently flexible to enable the companies to provide further services as pension trustees, investment fund trustees, and registered retirement savings plan trustees. In short, the companies appear to have stressed the provision of a wide range of loan services and investment facilities for the consumer. This trend has been enhanced by the establishment of networks of branch offices located in shopping centres and similar locations that are convenient for the consumer.

1.18 The past half century of trust company expansion has seen a corresponding evolution of legislation both by the federal government and the provinces for the protection of the depositing public. As a result the law is now a complex overlay of regulatory provisions, but the total effect has been, with a few exceptions,[20] to preserve successfully the stability of the companies. Problems of the permissibility of incorporation, borrowing powers, investment powers and regulation of the companies have received regular attention, and a departmental staff has been established with responsibility for supervising the activities of the companies. It would appear that the legislatures involved have, at least tacitly, acknowledged that the trust companies have become a vital part of the Canadian financial system.

Summary

1.19 A review of the history of loan and trust corporations and of the Ontario legislation presents some significant information to guide the making of decisions for the future:

(a) Building societies evolved in Ontario in response to the needs of the early colonists. As life became more complex they gave way to the more sophisticated loan corporation, and, having fulfilled their function, they disappeared from the financial scene.

(b) Loan corporations in their turn succeeded in accumulating British capital to help to satisfy the needs of the Canadian mortgage market.

When British capital became less accessible their expansion rate declined because they failed to compete aggressively with their competitors for intermediary funds in the domestic market. Despite their slow rate of expansion they still fulfil constant and useful functions, particularly in the accumulation of funds for residential mortgages.

(c) Trust companies have proved the amazing adaptability of the trust concept and its usefulness in serving the capital formation requirements of the consumer-public. The companies have shown an ability to respond to, and to expand to meet, the emerging needs of the day, and to compete effectively with other Canadian financial institutions including the chartered banks.

(d) In making legislative changes the Ontario Legislature should be mindful of the importance of strengthening loan corporations and trust companies as important financial institutions, and of encouraging their further development to serve the needs, particularly amongst the consumer-public, for highly efficient facilities for capital accumulation and capital borrowing and for efficient fiduciary services.

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1. Statutes of the Province of Canada, 9 Vic. (1846), c. 90.
2. One Hundred Years of Service: The Record of The Lambton Loan and Investment Company (Sarnia: 1944).
3. The Story of the Canada Permanent Mortgage Corporation, 1855-1925 (Toronto: 1925).
4. Statutes of the Province of Canada, 22 Vic. (1859), c. 53, section 36.
5. Statutes of Ontario, 38 Vic. (1875-6), c. 32.
6. Statutes of Ontario, 54 Vic. (1891), c. 38.
7. Statutes of Ontario, 60 Vic. (1897), c. 38.
8. See Neufeld, E. P., The Financial System of Canada (Macmillan; Toronto, 1972) at pp. 200-3.
9. Brief of The Trust Companies Association of Canada to the Select Committee on Company Law, December, 1974 at p. 10.
10. Halsbury's Laws of England, 3rd Edition, Vol. 38, p. 809 ff.
11. Neufeld, op. cit., Chapter 9, at p. 291.
12. Statutes of Ontario, 35 Vic. (1872), c. 83.
13. Statutes of Ontario, 45 Vic. (1882), c. 37.
14. Statutes of Ontario, 54 Vic. (1891), c. 33, section 1.
15. Statutes of Ontario, 60 Vic. (1897), c. 37. This Act was preceded two years earlier by The Trusts Companies' Act, 1895, Statutes of Ontario, 58 Vic. (1895), c. 32.
16. Statutes of Ontario, 2 Geo. V (1912), c. 34.
17. Statutes of Ontario, 11 Geo V (1921), c. 61.
18. Neufeld, op. cit., p. 315.
19. Neufeld, op. cit., p. 318.
20. See Report of the Royal Commission appointed to inquire into the failure of Atlantic Acceptance Corporation Limited, Vols. 1 - 4, September 12, 1969.

CHAPTER 2

The Legislation

2.01 The Committee's review of the law relating to loan and trust companies required a careful study of The Loan and Trust Corporations Act.[1] Throughout the present report this Act of the Ontario Legislature, as amended to date, is referred to as "the Act". The Act is derived from The Loan and Trust Corporations Act of 1912 and, although revised in 1949,[2] still retains much of the flavour of the 1912 statute. Ontario's loan and trust legislation has been the subject of frequent amendment over the years. The most recent amendments occurred in November, 1973, and December, 1974, while the work of the Committee was going on. The 1973 amendments made provision for "mortgage investment companies" which are a specialized type of loan company designed to stimulate the flow of funds to the residential housing market. The 1974 amendments made further important changes to the Act including provisions designed to increase the borrowing capacity of loan and trust companies by making possible the issue and sale of "subordinated notes". Due to the fact that the Committee had completed a major part of its work before introduction of the most recent amendments in November, 1974, there was insufficient time remaining to the Committee to review them in detail. The report does, however, contain some comment by the Committee with respect to certain new sections as well as comment on some of the general principles that appeared to be involved.

2.02 It is essential in any review of the Act to understand clearly at the outset that the Act is both an incorporation and registration statute. It provides for the incorporation of loan and trust companies in Ontario and for their registration to do business in the province. It also provides for the registration of federally incorporated companies and companies incorporated in the provinces that wish to carry on a loan or trust business in Ontario. Certain sections of the Act apply to all registered companies, while others apply only to some loan and trust companies, such as Ontario incorporated companies. These distinctions must constantly be borne in mind and will be the subject of frequent comment throughout the report. For ease of reference, the Committee will adopt defined terms which differ somewhat from those used in the Act. The expression "Ontario corporations" will be used to refer to loan and trust companies incorporated in Ontario; "federal companies" will be used to refer to loan and trust companies incorporated under Canadian federal legislation; and "extra-provincial companies" will be used to refer to loan and trust companies incorporated under the law of another province of Canada. It should

perhaps be emphasized that the expression "extra-provincial companies" when used in the report does not include loan or trust companies incorporated under foreign law.

2.03 Notwithstanding frequent amendments and the passing of a revised Act in 1949, the Committee considers that the loan and trust legislation of Ontario has not received comprehensive revision of the sort undertaken in legislation concerning business corporations in Ontario. As is well known, the corporation law of Ontario was extensively revised with the enactment of The Business Corporations Act in 1970.[3] The method of incorporation was changed from discretionary incorporation by issue of letters patent to incorporation as of right by issue of articles of incorporation, to mention but one of the important innovations of the new legislation. Although The Business Corporations Act does not apply to loan and trust corporations, the Committee was of the opinion that the principles underlying it should be used as a guide in its review of the Act and in formulating recommendations for new legislation. Consequently, throughout the report there are frequent references to The Business Corporations Act which for ease of reference is referred to simply as "the BCA".

2.04 The succeeding chapters of this report deal with specific matters relating to loan and trust corporations as, for example, matters relating to their incorporation and registration, and in each chapter the Committee makes recommendations for specific changes in the Act. The Committee wishes in addition to make the general recommendation that the Act should undergo a complete revision and updating at the present time. In its review of the Act, the Committee was struck by its complexity and by the need to cross-refer from one section to another in order to obtain the exact meaning of a particular section or provision. The Committee noted that while a number of sections simply used the defined term "corporation" (meaning a loan corporation or a trust company wherever incorporated in Canada), these sections had to be read subject to section 2 which significantly restricts their application. Section 2 would seem to constitute a trap to the unwary reader. The Committee would expect that some of these difficulties of interpretation will be eliminated in a revised new Act. During its deliberations, the question arose whether there should be frequent cross-reference to provisions in the BCA with respect to matters related to the internal affairs of loan and trust companies. The Committee has concluded that loan and trust corporations should continue to be governed in Ontario by their own separate statute and that recommended changes should be by way of amendments to the Act rather than by cross-reference to existing provisions of the general corporation statute. The Committee also considered the question of whether there should be separate statutes for loan and trust companies

as is the case federally and as used to be the case in Ontario prior to 1912. While some commentators[4] have expressed support for separate statutes, the Committee does not consider that it should make any recommendation in this regard and is content to leave this matter with the legislative draftsman of the new Act.

2.05 As already mentioned, for purposes of ease of reference, The Loan and Trust Corporations Act is referred to throughout the report as "the Act". The Committee has where possible and in accordance with its terms of reference, examined and taken account of legislation with respect to loan and trust companies enacted in the other provinces of Canada and at the federal level. The full citations of the relevant legislation are set forth below. When referring to the provincial or federal legislation in the report, the references will be simply to the particular province and not by way of full citation and in the case of the federal legislation, will be simply to the "Federal Acts".

Ontario

The Loan and Trust Corporations Act, R.S.O. 1970, c.254; as amended, 1971, c.98, section 4 and Schedule para. 20; 1972, c.101; 1973, c.128; 1974, c.88.

Alberta

The Trust Companies Act, R.S.A. 1970, c. 372; as amended, 1971, c.1 and c.109; 1973, c.57; 1974, c.14 and c.77.

British Columbia

Trust Companies Act, R.S.B.C. 1960, c.389; as amended, 1961, c.59, section 36; 1962, c.65; 1964, c.61; 1967, c.49, section 13; 1973, c.84, section 18.

Savings and Loan Associations Act, R.S.B.C. 1960, c.346; as amended, 1961, c.55.

Manitoba

The Companies Act, R.S.M. 1970, c.C-160; as amended, 1970, c.10; 1971, c.64; 1974, c.59.

New Brunswick

Trust, Building and Loan Companies Licensing Act, R.S.N.B. 1973, c.T-13.

Trust Companies Act, R.S.N.B. 1973, c.T-14.

Newfoundland

The Loan Companies and Finance Companies (Licensing) Act, 1961, S.N. 1961, No. 31; as amended, 1962, No. 36; 1973, No. 39 (Schedule C).

The Trust and Loan Companies (Licensing) Act, 1974, S.N. No. 120.

Nova Scotia

Trust Companies Act, R.S.N.S. 1967, c.316; as amended, 1969, c.80; 1970-71, c.62.

Loan Companies Act, R.S.N.S. 1967, c.171; as amended, 1968, c.36.

Loan Companies Inspection Act, R.S.N.S. 1954, c.158.

Trust and Loan Corporations Act, R.S.N.S. 1967, c.315 (this Act not proclaimed in force as at April, 1975. When Act proclaimed the Loan Companies Inspection Act is repealed).

Building Societies Act, S.N.S. 1951, c.2; as amended, 1954, c.54; 1962, c.19.

Prince Edward Island

An Act to Provide for the Licensing or Registration of Certain Corporations and Persons, S.P.E.I. 1971, c.25; as amended 1972, c.28; and regulations made May 19, 1971, November 24, 1971 and June 14, 1973.

Quebec

Trust Companies Act, R.S.Q. 1964, c.287; as amended, 1965, c.74; 1966-67, c.82, section 3; 1969, c.26, section 77; Bill No. 77, An Act to amend the Trust Companies Act, assented to December 13, 1974.

Loan and Investment Societies Act, R.S.Q. 1964, c.289.

Saskatchewan

The Trust Companies Act, R.S.S. 1965, c.132; as amended 1971, c.50.

The Loan Companies Act, R.S.S. 1965, c.133.

The Trust and Loan Companies Licensing Act, S.S. 1969, c.68.

Canada

Trust Companies Act, R.S.C. 1970, c.T-16; as amended, 1970 (1st Supp.), c.47; 1972, c.17, Schedule; 1974-75, c.7.

Loan Companies Act, R.S.C. 1970, c.L-12; as amended, 1970 (1st Supp.), c.24; 1972, c.17, Schedule; 1973-74, c.49; 1974-75, c.7.

2.06 **The Committee recommends that:**

(a) loan and trust corporations should continue to be subject to their own separate legislation in Ontario and that the Act relating to such corporations be completely revised and re-drafted consistent with the specific recommendations of this Report.

1. R.S.O. 1970, c. 254; as amended, 1971, c. 98, section 4 and Schedule para. 20; 1972, c. 101; 1973, c. 128; 1974, c. 88.
2. The Loan and Trust Corporations Act, 1949, S.O. 1949, c. 52.
3. R.S.O. 1970, c. 53; as amended 1971, c. 26 and c. 98, section 4; 1972, c. 1, section 30 and c. 138; 1974, c. 26.
4. See Report of the Royal Commission appointed to inquire into the failure of Atlantic Acceptance Corporation Limited, dated September 12, 1969, Vol. 3 at p. 1635.

CHAPTER 3

Incorporation

3.01 Loan corporations and trust companies are incorporated in Ontario by letters patent issued under the Act. This method of incorporation, which is discretionary, is the traditional method used in Ontario to incorporate companies of various kinds. The first significant change in the incorporation procedure occurred with the passing of the BCA which provides for incorporation as of right through the issue of articles of incorporation. Under the Act, application for incorporation of loan and trust companies is made by petition to the Lieutenant Governor in Council through the Minister of Consumer and Commercial Relations and delivered to the Registrar.[1] Prior to delivery of the application, the applicants must meet the following requirements: publication of notice of intention to incorporate;[2] the holding of a meeting of the promoters to constitute a provisional corporation, to adopt by-laws and to elect provisional directors[3]; payment in trust for the proposed corporation of at least $1,000,000 in subscribed capital by at least five responsible subscribers; and payment by each of the applicants for shares to an aggregate par value of at least $1,000.[4] Compliance with these requirements is established by declaration, affidavit and certified copy of the by-laws filed with the petition. Section 16 of the Act provides, in effect, that before letters patent of incorporation may be issued, the Lieutenant Governor in Council must be satisfied that: (a) there exists a public necessity for a trust or loan company, or for an additional trust or loan company, in the intended locality of the head office of the proposed company; (b) the fitness of the applicants to discharge the duties of a trust or loan company is such as to command the confidence of the public; and (c) the public convenience and advantage will be promoted by granting to the company the powers applied for. When the Lieutenant Governor in Council, that is the Cabinet, is satisfied as to the matters referred to in section 16, an order in council is passed authorizing the grant of letters patent. Letters patent are then issued bearing the signature of the Lieutenant Governor and the Minister and sealed with the Great Seal of the Province. Although under the Act the discretion with respect to the grant of letters patent lies with the Lieutenant Governor in Council, the role of the Minister and, in particular, of the Registrar in processing an application for incorporation is extremely important. The Committee was advised during its hearings that as a matter of practice, a petition for incorporation is not filed until after the promoters have met several times with the Registrar and his staff and have submitted such information as is required,[5] including a written brief outlining the proposed operations of the company

and containing other information. When the Registrar is satisfied that the requirements of the Act for incorporation will be met and agreement on the amount of the initial paid-in capital has been reached, the promoters proceed to publish notice of their intention to apply for incorporation, and in due course their petition to the Lieutenant Governor is filed with the Registrar. The Registrar reports on the petition to the Minister who, assuming that he is satisfied, recommends to the Cabinet that incorporation be granted.

3.02 In its review of the procedures to incorporate a loan or trust company in Ontario, the Committee considered the general question of whether the grant of incorporation should remain discretionary or whether it should, following the principle of the BCA, be granted as of right. It was drawn to the Committee's attention that during the ten-year period ended December 31, 1974, only three new loan or trust companies were incorporated in Ontario although, during the early 1960's a spate of new incorporations occurred.[6] This raised the question of a change to incorporation as of right in line with the procedure for incorporation under the BCA. What seemed to be significant to the Committee, however, was the very important role played by loan and trust companies as financial institutions, and, in the case of trust companies, their importance as corporate trustees. As financial institutions, loan and trust companies receive substantial sums of money from depositors and investors in their debentures, certificates and receipts, and the financial stability of these institutions is, in the Committee's opinion, of great importance to the residents of Ontario. While it is true that the Act imposes a substantial initial paid-in capital requirement and contains a number of other provisions designed to promote financial stability of these corporations, the Committee considers that control over entry into the loan and trust field must be preserved as an added safeguard to the public. The Committee does not consider that the ability of the promoters to satisfy the initial paid-in capital requirement assures the future financial success of the proposed corporation. In the view of the Committee, the promoters must also show that the new company will have at its disposal, particularly during the early years, the financial resources and management expertise necessary to create a viable operation. The Committee received no submissions in favour of granting incorporation as of right for loan or trust companies. A brief was received from The Trust Companies Association of Canada (hereinafter referred to as the "Association") urging that discretionary incorporation be retained. The Committee noted that incorporation of loan or trust companies under the Federal Acts and the applicable laws of the other provinces of Canada is discretionary without exception. Accordingly, the Committee concluded that incorporation of loan and trust companies in Ontario should continue to

be discretionary and not be as of right.

3.03 Having decided in favour of discretionary incorporation, the Committee considered the matter of choosing an appropriate forum for exercise of the discretion. The presence in section 16 of the phrase "the public convenience and advantage" caused some members to favour a committee of the Legislature as the proper forum to decide whether or not the granting of incorporation would promote the public convenience and advantage. Adoption of this approach would involve a change in procedure to incorporation by special act of the Ontario Legislature. It was noted that incorporation by special act is followed under the Alberta Act, the Saskatchewan Act, the Nova Scotia Acts and under New Brunswick law and is optional under the Federal Acts. Other members, while expressing support for this proposal, favoured retention of the existing procedure of incorporation by letters patent. It was pointed out that incorporation by letters patent has been available under the Federal Acts since 1970 and has been used on all new incorporations since that date.[7] The Committee decided on balance that incorporation by letters patent should be retained and that the discretion with respect to their issue should remain with the Lieutenant Governor in Council. The Committee considers, however, that the Act should be made more explicit with respect to the factors to be taken into account in exercising that discretion. While the Committee recognizes that decisions with respect to financial viability, responsibility of the subscribers and fitness to manage a loan or trust company are essentially subjective matters, the Committee considers that references to the "public convenience and advantage" and to "public necessity" should be deleted from the Act in favour of a more direct statement of the requirements for incorporation. The report now proceeds to deal with this conclusion in greater detail.

3.04 In the Committee's opinion, the following factors should be taken into account in reviewing an application for incorporation: (a) the fitness, both as to character and as to competence, of the proposed management (applicants, permanent directors and executive officers) to manage a loan or trust company; (b) assurance that the persons who own and are providing and control the funds put forward to finance the proposed company are themselves responsible; (c) assurance that a financially viable operation is proposed; and (d) the readiness of the promoters to offer a broad range of loan or trust services to the public. The Committee fully recognizes that there is a large element of discretion involved in each one of these four factors but it considers nevertheless that the very wide area of discretion that exists in the Act at present would be significantly narrowed if the requirements were thus more directly stated. The Committee wishes to emphasize its intent that if the four factors mentioned in this paragraph 3.04 are satisfied, then incorporation should

follow as a matter of course. Following this approach, the existing requirements to show public necessity and public convenience and advantage under section 16 would be abandoned. The Committee was advised by the Registrar that, notwithstanding the branch networks of loan and trust companies throughout Ontario today, it is still a fairly simple matter for an applicant to establish public necessity for a trust or loan company or for an additional trust or loan company in the intended locality of the head office of the proposed company, and that no application, certainly within the past ten years, had been refused on this ground. With regard to the other test, it appeared to the Committee to be exceedingly difficult, if not impossible, to state objective criteria against which to decide whether the "public convenience and advantage" would be served by granting or refusing a particular application for incorporation. Any decision on this ground runs the risk of being subjective and, as already noted, the Committee was concerned that the Act did not, as presently drafted, provide a proper forum for deciding a question of this nature. The Committee therefore recommends that section 16 be amended by deleting the requirements to show public necessity and public convenience and advantage. The Committee believes that some additional comment with respect to the fourth factor, readiness to offer a broad range of services to the public, is required. The Committee fully appreciates that a new loan or trust company may be required for competitive reasons to commence operations in a modest way. A company may start with only one office and engage in a limited area of activity. An example might be a trust company which limits its activities to acting as trustee for pension funds or registered retirement or home ownership savings plans and the sale of guaranteed investment receipts or certificates to the public. The Committee sees no objection to a company starting business in this manner. The longer range objective, however, in the Committee's view, must be to offer a gradually increasing range of loan or trust services to the public. The Committee is opposed to the incorporation of limited-purpose loan or trust companies whose sole intention and purpose is to serve the interests of a narrow group of persons or companies.

3.05 The Committee considered the question of whether an appeal should lie from a decision not to grant incorporation. The Act does not provide for an appeal. The only jurisdiction which grants an appeal at present is British Columbia which provides for an appeal to the Lieutenant Governor in Council from any decision of the Inspector refusing his consent to the incorporation of a company. The decision of the Lieutenant Governor in Council on such appeal is final and conclusive.[8] The Committee is of the opinion that a decision for or against the grant of incorporation is an administrative decision based

essentially upon matters of policy and that it would be inappropriate to provide for a right of appeal from a decision of the Lieutenant Governor in Council. Accordingly, the Committee recommends that there be no right to appeal a decision not to grant a petition for letters patent.

3.06 The Committee gave consideration to the minimum capital requirements in section 8. That section refers to a minimum paid-in initial capital of "at least $1,000,000". The Committee was advised that the usual practice is to require an amount of contributed surplus in addition to the $1,000,000 and that the amount required varies according to the proposed scope of operations. The Committee is opposed to retaining a statutory discretion with respect to the amount of the initial capital and believes that the Act should state the actual amount required. The Committee considers that, in the case of trust companies, the amount should be increased to $1,500,000 to take account both of inflation, since the existing amount was established in 1968, and of the departmental practice of requiring an additional amount of contributed surplus. The Committee also concluded that, if this recommendation is accepted, the departmental practice of requiring additional amounts of capital should be discontinued. For loan corporations, the Committee would retain the existing minimum of $1,000,000. This amount is already $500,000 higher than the amount required to incorporate a loan company under the Federal Acts. To increase the amount further would widen the disparity between the Ontario and federal legislation which the Committee considers would be an undesirable result. The departmental practice of requiring additional capital should be discontinued for loan corporations as well. The Committee approves and recommends retention of the present requirement whereby the full amount of the initial capital must be deposited in trust for the proposed company in a chartered bank branch in Ontario prior to filing of the petition for incorporation. The Committee was advised that the interval between incorporation and registration was normally three to four weeks for an Ontario corporation. As this is a relatively short period, the Committee did not consider it necessary to adopt the approach taken in the Federal Acts which permit the incorporators to pay the bulk of the minimum capital after incorporation but prior to registration.

3.07 Under existing procedures, an application for incorporation requires action by two offices of the Ministry: the Registrar's office and the Companies Division. A name search to determine the availability of the proposed corporate name is carried out by the Companies Division, which at a later stage also prepares the letters patent. The Committee is satisfied that the division of responsibilities between these two offices has worked well in practice and has not given rise to any significant delay. The Committee noted that the Act does not contain a section similar to

section 8 of the BCA with respect to the corporate name. Although, as a matter of practice, a petition filed under the Act is required to contain the customary statement of the applicants to the effect that the name is not such as is likely to deceive, the Committee finds it necessary to recommend that a section based on the principles of section 8 of the BCA be added to the Act and that it apply to all future applications for incorporation. The Committee also recommends the inclusion of a section similar to section 7 of the BCA which authorizes use of the corporate name in such language as the articles provide and as the Minister approves. The Committee believes that the pre-incorporation and organization procedures for loan and trust companies should be simplified and recommends that the requirement for a general meeting of the promoters be dispensed with.[9] There appears to be no justification for retaining this provision especially now that the Act requires a minimum of five subscribers only. In the Committee's opinion, it should no longer be necessary for the applicants to submit proposed by-laws with their petition. The by-laws should be passed in the customary manner following the grant of incorporation. This subject is discussed more fully in Chapter 12 of the report. The Committee recommends that the form of the petition be set forth in a schedule to the Act or be prescribed by regulation in order that it may be more readily available. The Committee also recommends that the requirement whereby a statutory meeting of the shareholders must be held not more than three months from the date at which the corporation is entitled to commence business be deleted from the Act.[10] This requirement appears to have been based on a provision of the Companies Act of Ontario as it existed when the Act was first enacted in 1912, and that provision appears to have been derived in turn from the English law.[11] Neither The Corporations Act nor the BCA provide for a statutory meeting and the Committee considers that it is a formality which can safely be removed from the Act.

3.08 Section 11 provides that incorporation may be granted without limitation of time, or for any limited term of years not less than ten. The Committee was advised that none of the 22 existing Ontario corporations is incorporated for a limited term and that if an application were to be received for incorporation for a limited term, it would in all probability be refused. The Committee is aware of no useful purpose to be served by retaining provision for limited term loan or trust companies and recommends that it be deleted from the Act.

3.09 **The Committee recommends that:**

(a) incorporation of a loan or trust company not be a matter of right but continue to be discretionary;

(b) incorporation of loan or trust companies in Ontario continue to be

by grant of letters patent, issued at the discretion of the Lieutenant Governor in Council following receipt from the incorporators of a petition for incorporation in the form to be set forth as a schedule to the Act;

(c) it no longer be necessary to show public necessity in the proposed locality of the head office or to satisfy a general test of public convenience and advantage;

(d) no appeal lie from a refusal to grant a petition for letters patent;

(e) incorporation of a loan or trust company be granted if the applicants can establish to the satisfaction of the Lieutenant Governor in Council that:

(i) the proposed management is fit, both as to character and as to competence, to manage a loan or trust company;

(ii) the persons who own and are providing and control the funds put forward to finance the proposed company are themselves responsible;

(iii) the proposed plan of operations is financially viable; and

(iv) the proposed corporation intends to offer initially or within a reasonable time after incorporation a broad range of loan or trust services to the public;

(f) the amount of the minimum initial capital be stated in the Act, there be no discretion with respect to the amount, the amount required for trust companies be increased to $1,500,000, and the amount required for loan corporations remain at $1,000,000;

(g) the Act should contain a section relating to the use and acceptability of proposed corporate names and comparable to sections 7 and 8 of the BCA;

(h) the requirement for a general meeting of promoters to be held prior to the filing of the petition for incorporation be dispensed with;

(i) the applicants no longer be required to file by-laws with their petition;

(j) section 18 of the Act, which provides for a statutory meeting of the shareholders, be deleted; and

(k) the provision for the incorporation of limited term loan or trust companies be repealed.

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1. The Act, section 3 (1).
2. The Act, section 3 (2) and (3).
3. The Act, section 3 (6).

4. The Act, section 8 (1).
5. The Act, section 3 (4).
6. As at December 31, 1974, there were eight Ontario incorporated loan corporations and 14 Ontario trust companies registered under the Act. Of these 22 companies, twelve or more than 50% were incorporated during the years 1961 - 1964 inclusive. The minimum initial paid-in capital stock during those years was $300,000. The minimum initial capital was increased to $500,000 in 1966 and to $1,000,000 in 1968. The three new companies were incorporated in 1969, 1972 and 1974 respectively.
7. Five new trust companies and one new loan company were licensed under the Federal Acts during 1971 through 1973. All were incorporated by letters patent issued under the Federal Acts.
8. Trust Companies Act, R.S.B.C. 1960, c. 389, section 27.
9. The Act, section 3 (5) and (6).
10. The Act, section 18.
11. The Companies Act, 1948, of the United Kingdom still provides for a statutory meeting of shareholders in section 130.

CHAPTER 4

Registration

4.01 Section 146 (1) of the Act provides that no incorporated body or person acting in its behalf, other than a registered corporation and a person duly authorized by it to act in its behalf, shall undertake or transact in Ontario the business of a loan corporation or of a trust company. Loan and trust companies wishing to undertake or transact a loan or trust business in Ontario must therefore register under the Act. The foregoing prohibition applies to Ontario corporations as well as to any loan or trust company carrying on business in Ontario whose jurisdiction of incorporation is outside Ontario. Registration involves compliance by a corporation with the requirements for admission in section 137 and submission of an application for initial registry to the Registrar under section 133. Section 133 also provides for the publication of notice of the application, the furnishing of such further material and evidence as the Registrar may direct, and the filing of a statement of the financial condition and affairs of the applicant corporation.[1] The Act imposes on the Registrar the duty of deciding which corporations are required to register and upon compliance with the provisions of the Act are entitled to registry.[2] Assuming that the Registrar is satisfied with the application and that all relevant requirements of the Act have been met, the Registrar enters the name of the corporation in the appropriate register maintained under section 120 and issues a certificate of registry to the corporation under section 135 (5). The certificate is granted on an annual basis and expires on the next June 30 following the date of its issue unless renewed upon application by the corporation.[3] Section 140 provides for an appeal from a decision of the Registrar with respect to a corporation's registration or right to registration under the Act.' At present the number of corporations registered under the Act is small. As at December 31, 1974, there were 64 registrants made up of 22 Ontario corporations, 28 federal companies, ten Quebec companies, two Alberta companies and two Manitoba companies.

4.02 The Committee considered the general question of who should be required to register under the Act. It would appear from the wording of section 146 (1) that only corporations are required to register. There was no indication given either at the Committee's hearings or in any of the submissions received that the Act was too narrow in its application or that it should be extended to cover a broader field. On the contrary, it appeared from the Committee's discussions that the Act may not be as precise as it should be in identifying the type of company which should

be required to register. No difficulty appeared to have been experienced in this regard with respect to trust companies. The number of trust companies incorporated in Canada is not large and it appeared to the Committee that the distinctive feature of these corporations, namely their right to exercise trust powers and to act as trustee, was not hard to identify. Registration questions involving trust companies therefore are largely matters of whether or not they are transacting their business in Ontario (apart of course from the important question of their eligibility to become registered in Ontario).[4] The Committee found it to be a much more difficult task, however, to identify a loan corporation within the meaning of the Act. The difficulty arises from the fact that the definition of "loan corporation" in section 1 (h) is very broad and appears to catch a good many corporations that are not registered under the Act. One result of the broad definition has been the need to create statutory exceptions to it which are to be found in section 3 (2) of the BCA and in section 2a of the Act itself. These exceptions are discussed in Chapter 5. The report now proceeds to examine the definition itself and to propose how it should be changed.

4.03 Loan corporations are defined in section 1 (h) as follows:

> "'loan corporation' means an incorporated company, association or society, constituted, authorized or operated for the purpose *of accepting deposits or issuing debentures, notes and like obligations and* of lending money on the security of real estate or investing money in mortgages, charges or hypothecs upon real estate or for those and any other purposes, but does not include a chartered bank, an insurance corporation, a trust company, a credit union incorporated under The Credit Unions Act, a company referred to in clause f of section 152 or clause g of section 155 and that is controlled by a loan corporation or a trust corporation in accordance with the regulations, or an investment company registered under The Investment Contracts Act;"[5]

The italicized words were added in 1974[6] with the result that the definition now takes account of the source of a loan corporation's funds as well as their use. Prior to this amendment, the definition referred only to the use made by a loan corporation of its funds. The Committee reviewed the history of section 1 (h) and noted that the wording respecting the use made by a loan corporation of its funds had been amended twice since the Act was first adopted. In the 1912 Act the operative words were "every incorporated company . . . constituted, authorized or operated for the purpose of lending money."[7] The definition was changed in 1949 when the Act was revised and under the changed definition the operative words became "every incorporated company . . .

constituted, authorized or operated for the purpose of lending money on the security of real estate."[8] A further change was made in 1970 when the phrase "or investing money in mortgages, charges or hypothecs upon real estate" was added to the definition.[9] While section 1 (h) of the Act as it now stands is a much clearer definition of a loan corporation than that presented in the 1912 Act, it appeared to the Committee that the definition is still too broad. Under the present wording, any corporation "constituted, authorized or operated for the purpose of . . . issuing debentures, notes and like obligations and of . . . investing money in mortgages" is caught. In order to arrive at a more precise understanding, the Committee considered the basic purposes of the Act.

It did not appear to the Committee that all corporations which borrow funds and invest or lend in mortgages should be regulated under the Act, and in fact, as already mentioned, some statutory exceptions to the Act already exist.[10] Nor did it appear to the Committee that the borrowing of funds from the public for the purpose of making mortgage loans was a sufficient reason for bringing under the Act all corporations that engage in that activity, because protection for the public is provided by the securities laws of Ontario when a corporation raises funds by the sale of its debt securities to the public. Again, the purpose of the Act is not to protect those who borrow from a loan corporation, as was conclusively shown by the illuminating judgment of Kelly J. A. in the important case of *Sidmay Ltd. et al v. Wehttam Investments Ltd.*[11] Kelly J. A., in rejecting the technical argument advanced on behalf of the borrower that a mortgage held by a corporation was unenforceable and void because the corporation had failed to register under the Act, examined the origin and purpose of the Act and the legislation from which it was derived. He concluded that the legislative purpose for bringing loan corporations under the Act was the intention to protect the money of the public, deposited with, loaned to, or invested in, such corporations for the purpose of enabling them to lend the money mainly on the security of mortgages on real estate.[12] The Committee agrees with the principle established by the Sidmay case that the purpose of the Act is to protect those who lend to a loan corporation and not those who borrow from it. In the Committee's opinion, however, a loan corporation should not be defined in the Act by reference to all persons who lend funds to the corporation, that is, depositors and debenture holders alike.

The Committee considers that the distinguishing feature of a loan corporation is its deposit-taking powers and this factor should, for definitional purposes, be used to distinguish a loan corporation from other corporations that borrow funds to invest in mortgages. In the opinion of the Committee, if such an approach were adopted, much of the confusion which appears to exist respecting which corporations are "loan

corporations" and which are not, would be removed and the need for statutory exceptions to the definition would be eliminated. The Committee therefore recommends that section 1 (h) be revised as follows:

> " 'loan corporation' means a company incorporated for the purpose of accepting deposits and of lending money on the security of real estate or investing money in mortgages, charges or hypothecs upon real estate or for those and any other purposes, and includes a mortgage investment company within the meaning of section 17a, but does not include a chartered bank, an insurance corporation, a trust company, a credit union incorporated under The Credit Unions Act, a company referred to in clause f of section 152 or clause g of section 155 and that is controlled by a loan corporation or a trust corporation in accordance with the regulations, or an investment company registered under The Investment Contracts Act."

4.04 Some additional comments with respect to the new definition proposed in paragraph 4.03 are required. The first concerns the phrase "incorporated company, association or society" in the present section 1 (h). It is not entirely clear whether the word "incorporated" modifies "association or society" in addition to "company". Since the Act requires incorporated bodies only to become registered and all existing registrants under the Act are corporations, the Committee assumes that "incorporated" is intended to modify the entire phrase. Therefore, in its new definition, the Committee proposes that the word "company" be substituted for the phrase "incorporated company, association or society". Secondly, the Committee wishes to comment on section 146 (2) which contains a statutory definition of what constitutes the undertaking of the business of a loan or trust corporation for purposes of the registration sections of the Act. Section 146 (2) was amended in 1972 by adding the phrase "or the advancing of funds of others in the purchase or lending on the security of mortgages that are assigned or registered in the name of the corporation." It would appear to the Committee that most companies which lend or invest money in mortgages would be caught by this phrase and as a result would be required to register under the Act. The Committee considers that the section as presently worded is too broad and that it also is in conflict with its proposed new definition of loan corporation. Accordingly, the Committee recommends that the phrase be removed from section 146 (2).

4.05 The Committee reviewed the provisions of the Act relating to admissibility to registry and the requirements for registry. Section 137 (1) provides that,

> "Trust companies whose powers do not include that of buying and selling land as beneficial owner except as authorized by this Act

and do not exceed the powers that are conferred upon trust companies under this Act and loan corporations that are solvent and fall within one of the following classes, may, upon due application, be admissible to registry:

1. Corporations duly constituted under the law of Ontario.
2. Corporations which, being duly incorporated or constituted under the laws of any other province of Canada, or of Canada, or of the United Kingdom, were in actual, active and bona fide operation in Ontario on the 16th day of April, 1912, but such corporations are admissible to registry only on due application and with the approval of the Minister and on such terms and conditions as he may prescribe.
3. Corporations duly constituted as joint stock corporations under the laws of any other province of Canada or of Canada that issue permanent shares having capital paid in and unimpaired of at least $1,000,000, together with such surplus as the Minister in the circumstances may require, and who undertake to comply with and be bound by the provisions of sections 54 to 59 to the same extent as if they were a provincial corporation."

The Committee notes that the opening words of section 137 (1) contain an ambiguity in that it is not clear whether the phrase "that are solvent and fall within one of the following classes" applies to both trust companies and loan corporations. The Committee reviewed the history of section 137 (1) and concluded that the phrase is intended to apply to both classes of corporation. Accordingly, the Committee recommends that the wording of section 137 (1) be revised to make this intent clear and to remove any possible ambiguity. With respect to the second class mentioned above, the Committee believes that section 137 (2) should also be deleted. The Committee considered the question of whether companies incorporated outside Canada should be permitted to register under the Act. The Committee noted in this connection that the Act no longer permits the incorporation in Ontario of a loan or trust company that is non-resident controlled[13] and it believes that this legislative purpose would be weakened if foreign corporations were permitted to register under the Act. Accordingly, the Committee recommends that corporations incorporated in Ontario or under the laws of any other province of Canada or under the laws of Canada be the only corporations that are permitted to register under the Act, which is what the Act substantially provides for today.

4.06 The provisions of the Act concerning the requirements for registration gave rise to some major questions to be answered by the Com-

mittee. They are discussed in this paragraph with reference only to federal companies and extra-provincial companies. Questions involving the registration of Ontario corporations are dealt with in paragraph 4.07. It was observed that the Act confers extensive discretionary powers on the Registrar and the Minister to grant or refuse an application for registry. While the Committee is confident that these powers have been responsibly exercised, it is nevertheless a matter of concern that such wide discretionary powers exist. Consistent with its conclusions on incorporation reached in Chapter 3, the Committee does not believe that it is appropriate to perpetuate the test that there should exist a public necessity for a trust company or for an additional trust company in the place in Ontario in which the applicant proposes to carry on business. Nor does the Committee consider it appropriate to retain the requirement that the public convenience and advantage be promoted by granting registration to the applicant corporation.[14] Therefore the Committee proposes that these requirements should be removed from the Act and that the requirements for registration should be made to conform as closely as possible to those for incorporating a loan or trust company in Ontario. The guiding principle should be the ability of the applicant corporation to meet the tests that would have been applied if it had sought to be incorporated in Ontario. These tests, as proposed by the Committee, are discussed in paragraph 3.04 above, and the Committee recommends that they be applied to corporations seeking registration in Ontario subject to the proviso that the third factor mentioned in paragraph 3.04, namely, that a financially viable operation is proposed, be replaced by a requirement that the Registrar must be satisfied with respect to the financial condition of the applicant. There are several further requirements which must be added in the case of applications for registration.

1. The corporation must be incorporated and licensed in good standing under laws of its jurisdiction of incorporation, which contain provisions that are substantially similar to those of the Act. The Committee is aware that uniformity of legislation does not exist between all provinces and that difficulties in applying this requirement could arise where, for example, an application is received from a loan corporation incorporated in one of the provinces that does not have loan corporation legislation. In such a case, the Committee believes that the Act should provide that the Registrar shall require an undertaking from the corporation to comply with the provisions of the Act.

2. The requirement in section 137 (1) 3 for capital paid-in and unimpaired of at least $1,000,000 should be retained, the amount increased in the case of trust companies to $1,500,000, and the words "at least" deleted. The phrase "together with such surplus as the Minister in the

circumstances may require" should, in the Committee's view, be deleted because of the recommended increase in unimpaired capital and the desire of the Committee to narrow the ambit of statutory discretion. The Committee also recommends that the test of solvency be deleted from section 137 (1) as being an unnecessary addition to the more basic requirement that the Registrar shall be satisfied as to the financial condition of the corporation.

3. The new requirement in section 137 (1) 3 for an undertaking to comply with the provisions respecting non-resident share ownership in sections 54 to 59 should be retained.

4. The requirements as to the power of attorney under section 134 and as to identical, deceiving, misleading or confusing names in section 136 (1) should also be retained.

5. There should continue to be a requirement to publish notice of the application[15] and to submit an application form and supporting information and material.[16] The Committee recommends that there be some tightening up of these provisions so as to reduce possible areas of discretion. The form of the application should be given in a schedule to the Act or prescribed by regulation; the amount of public notice should be specified and not left to the Registrar's discretion; and the Registrar's right to require the furnishing of further information, material and evidence should be limited to information, material and evidence relevant to the requirements for registration.[17] The Committee recommends that the defined term "due application" be deleted from section 1 and elsewhere in the Act, including section 137 (1), since this expression appears to introduce further discretion with respect to applications for registration. The requirement to pay registration fees should, however, be retained.

6. The requirement in The Ontario Deposit Insurance Corporation Act that a corporation wishing to accept deposits in Ontario must hold a policy of deposit insurance issued by the Canada Deposit Insurance Corporation should, of course, be retained.[18]

4.07 The Committee noted that under the Act, no Ontario corporation may undertake or transact in Ontario the business of a loan corporation or of a trust company unless it is registered.[19] Section 133 which deals with applications for initial registry applies to Ontario corporations as well as to federal and extra-provincial companies. Ontario corporations are admissible to registry if they are solvent. Under the present practice, an Ontario corporation is required to publish notice of its intention to seek registry, must submit an application to the Registrar and satisfy him that there has been no impairment of capital since the date of incorporation, no material change in the management of the corporation

and no change in shareholder control. The Committee recommends that these provisions be retained, that the application form to be completed by an Ontario corporation be set forth in a schedule to the Act or prescribed by regulation, that the form require the applicant to furnish information concerning management, paid-in capital and controlling shareholders, and that the Registrar should have a discretion to reject the application if there has been any material change since the date of incorporation. The Act is not clear as to the exact powers an Ontario corporation may exercise prior to becoming registered under the Act. The Committee considers that its exercise of powers should be limited to the taking of such action as is required to organize the corporation and recommends that a section similar to section 11 of the Alberta Act be added to the Act.[20] The Committee also recommends that section 13 be amended so as to impose an affirmative obligation upon an Ontario corporation to become registered under the Act within two years after incorporation, failing which its corporate powers, save those necessary to effect its winding up, shall be forfeited and the corporation shall be obligated to commence winding up proceedings.

4.08 The Act requires all corporations to renew their registrations on an annual basis.[21] The Committee believes and recommends that the requirements for initial registry should be continuing requirements to be satisfied at the time of each annual renewal. To reinforce this recommendation, the Committee proposes that a new subsection be added to section 135 conferring on the Registrar power to insist that any corporation furnish information relevant to these continuing requirements. With respect to the paid-in capital requirement, however, the Registrar should be given a discretion to renew or refuse registration where there has been an impairment of capital depending upon his assessment of the seriousness of the impairment. This would take the place of the solvency requirement in section 135 (7) because, in the Committee's opinion, any impairment which renders a corporation insolvent should result in its registration not being renewed. Provision should be made in the Act to exempt corporations already registered under the Act from having to satisfy the Registrar as to their readiness to offer a broad range of loan or trust services to the public. This requirement should only apply to corporations seeking initial registry after the new Act comes into force.

4.09 It follows from the Committee's recommendations in paragraph 4.06 that if a corporation satisfies the requirements for registration, it is entitled to full registry. The Committee understands that at present relatively few corporations have been registered on a "limited" or "restricted" basis which precludes them from engaging in certain areas of activity such as, for example, the receipt of deposits or the issue of

guaranteed receipts or certificates. Authority to impose terms and conditions on the registry of federal and extra-provincial companies is conferred on the Minister by section 137 (3). In the Committee's opinion, limited or restricted registry is undesirable and should be discouraged, and the Committee recommends that section 137 (3) be deleted from the Act. In making this recommendation, the Committee intends that the provision for deposit of approved securities with the Minister under section 137 (3) should be deleted since it appears to the Committee that it is rarely used and is of doubtful value. The Committee's recommendation should not be taken, however, as extending to the Minister's power to impose limitations or conditions on the registry of an Ontario corporation which is unable to account satisfactorily for any assets that appear on its books.[22] The Committee believes that the imposition of limitations or conditions on such a corporation's registry may well be appropriate in such circumstances.

4.10 Section 121 (1) provides that,

> "The duty of determining, distinguishing and registering the corporations that under this Act are required to be registered and are entitled to registry, and of granting registry accordingly, is upon the Registrar, subject to appeal as provided in section 140."

and section 139 provides that,

> "Where in any disputed case the Registrar decides that a corporation is or is not legally entitled to registry, or to renewal of registry, or where he suspends, revives or cancels the registry of a corporation, his decision, except as otherwise provided, shall be given in writing, and he shall cause a copy thereof certified under his seal of office to be delivered to the corporation."

Finally, section 140 provides, in effect, that the corporation may request a hearing and review of the matter by the Registrar, that the Registrar may hear certain evidence in the review, that the Registrar is empowered to confirm, revoke or alter his former decision, and that an appeal from the review may be made to a judge of the Court of Appeal. The Committee is of the opinion that while there should continue to be an appeal from any decision of the Registrar within section 139, it should not be to the Registrar in the first instance. The Committee believes that the appeal from the Registrar's decision should be to an independent tribunal such as The Commercial Registration Appeal Tribunal constituted under The Ministry of Consumer and Commercial Relations Act.[23] Section 9b (1) of that Act provides for an appeal from a decision or order of the Tribunal to the Supreme Court. The Committee therefore recommends that section 140 be deleted and a new section substituted

therefor providing for an appeal from a decision of the Registrar under section 139 to The Commercial Registration Appeal Tribunal.

4.11 **The Committee recommends that:**

(a) the definition of "loan corporation" be changed as recommended in paragraph 4.03;

(b) section 146 (2) of the Act be amended by deleting the phrase "or the advancing of funds of others in the purchase or lending on the security of mortgages that are assigned or registered in the name of the corporation";

(c) registrants under the Act be limited to loan and trust corporations incorporated under the laws of Ontario or any other province of Canada or under the laws of Canada;

(d) the requirements for registration of federal and extra-provincial companies should conform as closely as possible to the requirements for incorporating a new loan or trust company in Ontario which are set forth in paragraph 3.04;

(e) in addition to the requirements in (d) above, federal and extra-provincial loan and trust companies should satisfy the following requirements in order to be registered in Ontario, namely, that they:

  (i) be incorporated and licensed under laws of the home jurisdiction substantially similar to the Act, or alternatively, undertake to the Registrar to comply with the provisions of the Act;

  (ii) have unimpaired paid-in capital of $1,500,000 for trust companies and $1,000,000 for loan companies;

  (iii) undertake to comply with sections 54 to 59 of the Act;

  (iv) submit a power of attorney as required by section 134 and comply with the corporate name provisions in section 136;

  (v) give such notice of the application as the Act shall expressly require, submit an application in the form to be set out in the Act and submit such supporting information and material as is required by the form; and

  (vi) be the holder of a policy of deposit insurance issued by the Canada Deposit Insurance Corporation or have their deposits insured in some other manner approved by the Lieutenant Governor in Council should they intend to accept, receive or issue deposits in Ontario;

(f) extra-provincial trust companies no longer be required to show public necessity or to establish that the public convenience and advantage will be promoted by granting registry;

(g) the application form to be completed by an Ontario corporation should be set forth in the Act or regulations and the Registrar should have a discretion to refuse the application where there has been a material change in management, paid-in capital or shareholder control since the date of incorporation;

(h) the requirements for initial registry should be continuing requirements to be satisfied at the time of each annual renewal;

(i) corporations should not be granted limited or restricted registry; section 137 (3) should be repealed; and

(j) an appeal should lie to The Commercial Registration Appeal Tribunal from any decision of the Registrar under section 139.

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1. The Act, section 133 (2) and (3).
2. The Act, section 121 (1).
3. The Act, section 135 (7).
4. For a case dealing with the question what constitutes the undertaking of a trust business in Ontario see Montreal Trust Company v. Abitibi Power & Paper Company (1937) O.R. 939.
5. The Act, section 1 (h).
6. The Loan and Trust Corporations Amendment Act, 1974, S.O. 1974, c. 88, section 1 (1).
7. The Loan and Trust Corporations Act, S.O. 1912, c. 34, section 2 (7).
8. The Loan and Trust Corporations Act, 1949, S.O. 1949, c. 52, section 1 (h).
9. The Loan and Trust Corporations Amendment Act, 1970 (No. 2), S.O. 1970, c. 129, section 1 (3).
10. The BCA, section 3 (2); the Act, section 2a. A further exception is contained in section 4 (3) of The Corporations Act, R.S.O. 1970, c. 89. The Committee was advised that it is the policy of the Companies Division not to permit any new corporations to be incorporated under section 4 (3) of The Corporations Act.
11. (1967) 1 O.R. 508 reversing a judgment of Grant J., (1966) 1 O.R. 457, which held the mortgage illegal and void by reason of the mortgagee's failure to register under the Act. The appeal to the Supreme Court of Canada was dismissed, (1968) 69 D.L.R. (2d) 336.
12. (1967) 1 O.R. at p. 523.
13. The Act, section 55 (3).
14. The Act, section 137 (4).
15. The Act, section 133 (2).
16. The Act, section 133 (1).
17. The Act, section 133 (2).
18. The Ontario Deposit Insurance Corporation Act, R.S.O. 1970, c. 307, section 23 (1).
19. The Act, section 146 (1).
20. See the Alberta Act, section 11 which provides:
    "Until it is registered and has received its certificate of registration, a company shall not commence business and shall not exercise any of its powers except for purposes in connection with its organization under this Division and its application for registration."
21. The Act, secton 135 (7).
22. The Act, section 130 (2) (a).
23. Enacted as The Department of Financial and Commercial Affairs Act, R.S.O. 1970, c. 113; as amended 1971 c. 50, section 28; 1972 c.1, section 23 (name of Department changed to The Ministry of Consumer and Commercial Relations); 1973 c. 95, section 1.

CHAPTER 5

Exceptions To Registration

5.01 As indicated in paragraph 4.02, certain statutory exceptions to the definition of loan corporation exist. The principal exception is to be found in section 3 (2) of the BCA which permits the incorporation of so-called "3 (2) corporations" that have power to lend and invest money in mortgages. Section 3 (2) provides as follows:

> "3 (2) Notwithstanding subsection (1), a corporation may be incorporated under this Act with power only to lend and invest money on mortgage of real estate or otherwise, or with power only to accept and execute the office of liquidator, receiver, assignee, trustee in bankruptcy or trustee for the benefit of creditors and to accept the duty of and to act generally in the winding up of corporations, partnerships and estates, other than estates of deceased persons, and shall not by reason thereof be deemed to be a corporation within the meaning of The Loan and Trust Corporations Act, but the number of its shareholders, exclusive of persons who are in the employment of the corporation, shall be limited by its articles to five, and no such corporation shall issue debt obligations except to its shareholders, or borrow money on the security of its property except from its shareholders, or receive money on deposit or offer its securities to the public."

It will be seen that section 3 (2) provides for two types of corporation; the first having power only to lend and invest money on mortgage of real estate or otherwise, and the second with power only to accept and execute the office of liquidator and the other offices thereafter specified in the section. The first type will be hereafter referred to as "private loan corporations" and the second type as "liquidator companies".[1]

5.02 Section 3 (2) is derived from a 1926 amendment to The Ontario Companies Act which permitted companies to be incorporated under that Act with power to lend and invest money on mortgage or real estate or otherwise[2]. An amendment of this nature was required if such a company was to be permitted incorporation under the general companies statute because the purposes for which companies could be incorporated under the general statute did not include the purposes of corporations within the meaning of The Loan and Trust Corporations Act.[3] The amendment imposed certain restrictions on private loan corporations. They must be private companies; the number of their shareholders is limited to five; borrowings are restricted to borrowings from the companies' shareholders; and the company is prohibited from receiving money on deposit.

These restrictions have in essence continued to the present day as will be seen from an examination of section 3 (2) of the BCA. It appeared to the Committee that fairly extensive use has been made of section 3 (2) over the years. The Committee was advised by the Companies Division that as at December 12, 1973, there were 546 private loan corporations in existence; a large number when compared with the number of Ontario incorporated loan corporations registered under the Act, namely eight in total. The Committee understands that in some instances, the controlling shareholder of a private loan corporation is itself a corporation and that the parent corporation may borrow funds for the purpose of making loans to its private loan corporation subsidiary. Such borrowings would, of course, have to be made in compliance with the securities laws which may require the parent corporation to file a prospectus. The Committee also understands that the parent corporations are sometimes financial institutions such as finance companies, many of which have private loan corporation subsidiaries. When looked at on a group basis, a private loan corporation which has a financial institution as its controlling shareholder and which borrows from its parent (the funds having been borrowed by the parent in turn from the public), would seem to be transacting the business of a loan corporation within the broad definition of that term in section 1 (h) of the Act. This would seem to raise the question whether section 3 (2) provides a means to circumvent the Act. The Committee considers that this question has already been answered by its recommendation in paragraph 4.03. There is no circumvention of the Act because neither the private loan corporation nor its shareholders may receive deposits from the public and this fact, in the Committee's view, is what distinguishes them from a loan corporation. Protection to those who lend funds to the parent shareholder is, and in the Committee's opinion, should be afforded by the securities laws and the need for additional regulation under the Act disappears. It also follows that if the proposed new definition of loan corporation is adopted, the need for section 3 (2) also disappears because it will then be possible to incorporate under section 3 (1) of the BCA an ordinary business corporation that has power to invest and lend money on mortgages.[4]

5.03 The Act was amended in 1974 to create two new exceptions to the definition of loan corporation.[5] The first exception is found in section 2a (a) which provides:

> "2a. This Act does not apply to,
>
> (a) an incorporated company that is authorized, constituted or operated for the purpose of lending money on the security of real estate or investing money in mortgages, charges or hypothecs upon real estate that does not accept deposits, and borrows only by way of,

(i) loans from chartered banks in the usual course of business, or

(ii) by the issue of debentures, notes, or like obligations of an amount not less than $100,000 each to any one person on his account, whereby the company is not obligated, or by demand of the holder cannot be obligated, to repay the money secured by such a debenture, note or like obligation within five years from the date of the issue of the said debenture, note or like obligation;"

This section when read together with section 3 (1) of the BCA would appear to open the possibility of incorporating a corporation under section 3 (1) of the BCA whose purpose is to lend or invest money in mortgages on real estate and whose articles limit its ability to borrow funds in the manner specified by paragraphs (i) and (ii) of section 2a (a). It appeared to the Committee that the distinctive feature of corporations within the new exception when compared to private loan corporations is that the former can borrow funds from chartered banks and (subject to the limits as to minimum amount and early maturity) from any other person, whereas private loan corporations may only borrow from their shareholders. It would seem that the amendment is intended, in part at least, to provide an alternative to the private loan corporation which would not be subject to the restrictions that apply to such a corporation. The second exception is contained in section 2a (b) which provides as follows:

"2a. This Act does not apply to, . . .

(b) an incorporated company whose objects do not provide for the lending of money on the security of real estate or leaseholds or the investing of its funds in mortgages or hypothecs on real estate or leaseholds and that acquires the bonds, debentures, debenture stock or other securities of a company that are collaterally secured wholly or in part by a mortgage or hypothec upon real estate or leaseholds."[6]

It would seem to the Committee that the purpose of this section is to remove any possible doubt that a corporation, which takes as collateral security for a loan made by it to another company, mortgages on real estate, might be considered to be a loan corporation within the definition.

5.04 The Committee is concerned that uncertainty in the definition of loan corporation should have given rise to three separate exceptions to the Act. In the Committee's opinion, none of these exceptions would be required if the definition proposed by the Committee in paragraph 4.03

were adopted. The Committee is also of the view that the restrictions imposed by section 3 (2) of the BCA upon private loan corporations and the restrictions imposed by section 2a of the Act should not be retained as statutory restrictions. The Committee believes that corporations should be encouraged to lend mortgage funds in Ontario. Persons wishing to form a corporation having power to invest or lend on mortgages should be permitted to incorporate in the normal way under section 3 (1) of the BCA, free from any special restrictions under section 3 (2) of the BCA or under the exceptions created by section 2a of the Act. Should such a corporation wish to borrow from the public under a prospectus, it should be a matter for the Ontario Securities Commission to determine whether any restrictions with respect to such matters as liquidity or financial stability should be imposed upon the corporation. The Committee therefore recommends that upon adoption of its proposed definition of loan corporation, no new corporations be incorporated in Ontario under section 3 (2) of the BCA or section 2a of the Act, and that any corporation that wishes to invest or lend on mortgages but does not seek the power to accept deposits from the public should be incorporated in the normal way under section 3 (1) of the BCA.

5.05 Lest there be any uncertainty as to the intended effect of its recommendations, the Committee wishes to state expressly that any corporation coming within its proposed new definition of a loan corporation and being registered under the Act should continue to enjoy the special exemptions afforded to loan corporations under The Securities Act.[7] Under section 19 (2) 1 of The Securities Act, registration is not required to trade in "bonds, debentures or other evidences of indebtedness . . . of . . . a trust company or loan corporation registered under The Loan and Trust Corporations Act . . .". Section 58 (2) of The Securities Act goes on to provide, in effect, that no prospectus need be filed with the Ontario Securities Commission in order for a person or company to trade in such securities. The Committee is of the opinion that these exemptions should continue to apply to loan and trust companies registered under the Act. To provide otherwise would, in the Committee's opinion, be undesirable since this would unnecessarily subject these companies to dual regulation under separate statutes.

5.06 As mentioned in paragraph 5.01, section 3 (2) also provides for the incorporation of liquidator companies. This provision has existed since 1953. No information was made available to the Committee as to the number of liquidator companies in existence. Liquidator companies are subject to the same restrictions as to number of shareholders and borrowing powers as private loan corporations. The Committee is of the opinion that the exception for liquidator companies belongs more

properly in the Act and therefore recommends that the definition of trust company in the Act be amended as follows:

> "1 (p) 'trust company' means a company constituted or operated for the purpose of acting as trustee, bailee, agent, executor, administrator, receiver, liquidator, assignee, guardian of a minor's estate, or committee of a mentally incompetent person's estate but does not include a company constituted or operated solely for the purpose of accepting and executing the office of liquidator, receiver, assignee, trustee in bankruptcy or trustee for the benefit of creditors and of accepting the duty of and acting generally in the winding up of corporations, partnerships and estates, other than estates of deceased persons."

Corporations wishing to have the limited powers of a liquidator company should henceforth be incorporated under section 3 (1) of the BCA.

5.07 **The Committee recommends that:**

(a) corporations which do not have the power to accept deposits from the public but have the power to lend and invest money on mortgages of real estate or otherwise, should henceforth be incorporated as ordinary business corporations under section 3 (1) of the BCA and should have all the powers of a business corporation under that Act;

(b) upon adoption of the new definition of loan corporation as proposed by the Committee in paragraph 4.03 of the report, no new corporations should be incorporated under section 3 (2) of the BCA or under section 3 (1) of the BCA with articles limiting their powers as provided in section 2a of the Act;

(c) corporations registered under the Act should continue to enjoy the exemptions contained in sections 19 (2) 1 and 58 (2) of The Securities Act; and

(d) the definition of trust company in section 1 (p) of the Act should be amended to except therefrom liquidator companies as presently defined in section 3 (2) of the BCA and any new liquidator companies should thereafter be incorporated under section 3 (1) of the BCA.

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1. The liquidator company exception was created when a new Corporations Act was enacted in 1953. See S.O. 1953, c. 19, section 3 (2).
2. Section 2, S.O. 1926, c. 48, reads as follows:
"2. Section 3 of The Ontario Companies Act is amended by adding thereto the following subsection,—

(2) Notwithstanding anything in the first subsection contained a private company may be incorporated under this Act with power to lend and invest money on mortgage or real estate or otherwise, and shall not by reason thereof be deemed a corporation within the meaning of The Loan and Trust Corporations Act, but the number of its shareholders shall be limited by its Letters Patent or Supplementary Letters Patent to five, and no such company shall issue bonds, debentures or debenture stock, or borrow money by the hypothecation of its securities except from the shareholders of the said company or receive money on deposit; provided that any such company shall be liable to payment of taxes as a loan corporation under section 4 of The Corporations Tax Act."

3. The Ontario Companies Act, R.S.O. 1914, c. 178, section 3.
4. The BCA, section 3 (1) provides:
"A corporation may be incorporated under this Act for any lawful objects to which the authority of the Legislature extends, except those of a corporation the incorporation of which is provided for in any other Act."
5. The Loan and Trust Corporations Amendment Act, 1974, S.O. 1974, c. 88, section 2.
6. The Loan and Trust Corporations Amendment Act, 1974, S.O. 1974, c. 88, section 2.
7. The Securities Act, R.S.O. 1970, c. 246, as amended by 1971, c. 31; 1972, c. 1; and 1973, c. 11, sections 19 (2) 1 and 58 (2).

CHAPTER 6

Objects and Powers

6.01 Throughout its hearings the Committee had the opportunity to question industry representatives and the Registrar and his staff concerning the nature and scope of loan and trust company operations today. At the request of the Committee, the Association, which represents approximately one-half of the loan and trust companies registered in Ontario, was represented at the hearings by its officers and from time to time by senior officers of several of its members. The Association arranged for knowledgeable representatives of the industry with experience in the specialized fields of company operations to appear before the Committee; these fields included financial intermediation, administration of estates and trusts, corporate trustee and transfer agent, pension trustee, and real estate agent. The information received from these representatives as well as from the Association representatives and those responsible for the administration of the Act was most helpful to the Committee. Hearings of the Committee were also held in New York City and London, England, where the Committee heard from representatives and regulators of the comparable financial institutions in New York State and England. As a result the Committee gained a good understanding of the role of loan and trust companies as financial institutions in Canada and some useful comparisons with financial institutions in two important foreign jurisdictions.

6.02 It appeared to the Committee that loan corporations are unique as financial institutions. They are distinguishable from other institutions in that their business consists almost exclusively of the twin functions of raising funds (through taking deposits and selling debentures) and of lending or investing their funds in mortgages, primarily on residential properties. The essence of their business is financial intermediation and the object to which that function is directed, namely mortgage lending, is obviously of great importance to the residents of Ontario. (Financial intermediation will be discussed more fully in Chapter 7.) The closest American comparison appeared to be the numerous savings and loan associations incorporated under either state or federal law. These associations are also important mortgage lenders but are distinguishable from Canadian loan corporations on a number of grounds. Most savings and loan associations are organized in mutual corporate form as opposed to capital stock corporate form and the members are the depositors who have voting rights based on the amounts deposited in a savings account with the association.[1] Another difference is that federal savings and loan associations and state savings and loan associations, which are

federally insured and supervised, have, since 1966, been subject to federal statutory control which fixes the amount of interest they may pay to depositors on their savings accounts.[2] In contrast to loan corporations in Canada, deposits with savings and loan associations, which constitute the bulk of their funds, are ordinarily withdrawable at any time without notice. In England, the building societies provided the closest parallel, but the differences between these institutions and loan corporations appeared to the Committee to be more significant than their similarities, despite the historical links between both classes of institution as outlined in Chapter 1. Most of a building society's funds are raised through share subscriptions from a great number of individual subscribers[3] and these subscriptions are, under normal conditions, withdrawable at any time without notice or on very short notice.

6.03 The number of loan corporations registered in Ontario today is not large, 26 corporations as at December 31, 1974, and of these registrants the largest companies are incorporated under the Federal Acts or extra-provincially. The Committee was advised that during the early 1960's, a number of new loan corporations were incorporated in Ontario and that these corporations are functioning successfully today either as separate corporations, amalgamated corporations or as subsidiaries of trust companies. While the Committee considers that loan corporations should be encouraged in Ontario, no general proposals to this end were put forward by the individual companies themselves or by the Association in its submissions to the Committee. It occurred to the Committee that the recent amendments to the Act which will permit loan corporations to issue subordinated notes should provide an incentive to the existing companies and may encourage the formation of new loan corporations. The Committee also noted the 1973 amendments to the Act which permit the incorporation of specialized companies known as "mortgage investment companies" (existing loan corporations may also opt for this status) and it appeared that these amendments may also encourage the formation of new companies. The Committee has concluded that all of the salient functions served by building societies and savings and loan associations in England and the United States are performed by our existing financial institutions, and, in particular, by loan and trust companies. Therefore, the Committee did not consider that it should recommend the enactment of new legislation designed to encourage the incorporation of building societies or savings and loan associations in Ontario.

6.04 The Committee is of the opinion that the term "loan corporation" is not sufficiently descriptive of the role of loan corporations. Most existing companies have the word "mortgage" as part of their name and the Committee recommends that the Act be amended to refer to loan corporations as "mortgage loan corporations". Unlike trust companies

whose powers are specified in section 84, the Act does not contain a section setting forth the powers of a loan corporation. In the Committee's opinion, such a section should be included and the Committee recommends the following:

> "Subject to the provisions of this Act, a provincial loan corporation may and any other registered loan corporation that has the capacity to do so may:
>
> (a) accept deposits and issue debentures, notes and like obligations for any moneys borrowed by the corporation;
>
> (b) lend money on the security of real estate or invest money in mortgages, charges or hypothecs upon real estate; and
>
> (c) act generally as agent for the transaction of business, the collection of loans, rents, interest, dividends, mortgages and other securities for money, as a depository for the safekeeping of securities and personal property and to carry on the business of a mortgage or real estate broker."

Under a 1970 amendment to the Act,[4] Ontario loan corporations were empowered to apply by petition to the Lieutenant Governor in Council for an order authorizing them to exercise agency powers. These powers, which appear to the Committee to be very broad and to have been derived from section 84 (d) of the Act, are reproduced in clause (c) above. The Committee was advised that several corporations have applied for and received orders authorizing them to exercise agency powers.[5] Such loan corporations may act as agent in a variety of capacities including agent to collect and administer mortgage loans; to receive property for safekeeping; and to act as a mortgage broker. The Committee concurs with this enlargement of a loan corporation's powers and recommends (a) that the requirement to obtain an order in council prior to the exercise of agency powers be deleted and (b) that all loan corporations registered under the Act, be empowered to exercise agency powers in Ontario provided that they have the capacity to do so under the laws of their jurisdiction of incorporation.

6.05 The Committee considered the question of whether Ontario loan corporations should be permitted to apply for trust powers. The Committee was of the opinion that the distinction between a loan corporation and a trust company should be preserved and therefore recommends that no change be made in the Act to permit Ontario loan corporations to apply for trust powers.

6.06 Trust companies were also found by the Committee to be unique as financial institutions. Chapter 1 has dealt with the history of trust companies in Canada. The Committee found that in New York State

the trust services of trust companies were performed by the large commercial banks through their "trust departments". Commercial banking and trust work is carried on within the same corporate entity in contrast to the division of functions between different corporate entities in Canada. The Committee was advised that there are very few "pure trust companies" in the United States, that is, trust companies which do not engage in commercial banking. The large clearing banks in England also have trust departments which offer a trust service. In addition, certain of the merchant banks have "trust corporation" subsidiaries and there are several well known "trust corporations" in England which act principally as trustee of corporate security issues.

6.07 The picture that emerged of present day trust company operations in Ontario showed that these companies offer a broad range of financial services to the public, in most cases through departments or divisions of the same corporate entity, and in some cases through specialized subsidiaries. Links between trust companies and loan corporations are frequent, with some of the well-known trust companies having their own loan corporation subsidiaries or being themselves subsidiaries of loan corporations. The services offered include the administration of wills and estates, acting as trustee, acting as agent including real estate broker, pension trustee, registrar and transfer agent for companies and trustee of corporate issues, and acting as a financial intermediary. (The financial intermediary function will be dealt with more fully in Chapters 7 and 8 and the traditional role of trust companies as executor and trustee of wills and estates more fully in Chapter 9.) Not all trust companies offer the full range of service but most of the large ones do. This broadening of functions has tended to bring trust companies into increasing competition with other financial institutions, such as the banks, insurance companies and finance companies, which have also been broadening their activities.

6.08 As is to be expected, the statement in the Act of a trust company's objects and powers is extremely wide. It is found in section 84 which, considering that it was enacted in 1912 and has had remarkably few amendments since, has shown great resiliency over the years. It appeared to the Committee that this was due in part to the fact that the broad powers conferred under section 84 must be read in the context of the later sections of the Act which limit both the borrowing powers and the investment powers of trust companies. It is in these later sections where most of the legislative changes have occurred and where today most of the legislative refinements are to be found. (Borrowing powers are discussed more fully in Chapter 7, and Chapter 10 deals with investment powers.)

6.09 The Committee does consider that in any redraft of the Act an attempt should be made to modernize the language of section 84. In stating the objects of trust companies, this section does not use many of the expressions which describe what trust companies in fact do. In the Committee's opinion, the section would be improved if it referred to a company that acts as registrar and transfer agent, disbursing agent, real estate agent and pension trustee, to give several examples. The Committee is also of the opinion that clause (h) should be deleted because trust companies do not guarantee investments made by them so far as the Committee is aware. In the Committee's opinion, certain of the incidental powers contained in section 15 (1) of the BCA should be added to the powers of Ontario corporations under the Act. In order to provide a point of reference for further discussion, the Committee proposes that section 84 be changed in accordance with the draft section set out in the Appendix to the report. The incidental powers suggested by the Appendix should also be granted to Ontario loan corporations.

6.10 The Committee understands that when the Act was revised in 1949, a section was added (now section 96) which confers on Ontario corporations "the general capacity that the common law ordinarily attaches to corporations created by charter". The Committee is of the view that the purpose of this section is to remove any possibility that the doctrine of ultra vires might apply to Ontario corporations. The section is followed by section 97 which deals with the matter of the exercise by an Ontario corporation of its powers beyond Ontario. In the Committee's opinion, these two sections should be retained in the Act without amendment.

6.11 The Committee noted that section 105 of the Act provides that an Ontario corporation may have a seal for use outside Ontario. The Committee has no objection to this section but questions whether it is required in the Act. The Committee considers that a properly drawn by-law provision should be sufficient and therefore recommends that section 105 be deleted.

6.12 **The Committee recommends that:**

(a) no new legislation be enacted in Ontario at this time to encourage the formation of building societies or savings and loan associations based upon the British and American models;

(b) a new section be added to the Act describing the powers of a loan corporation;

(c) all loan corporations registered under the Act should be free to exercise the agency powers described in section 17 without first having to obtain an order in council;

(d) loan corporations should not be permitted to apply for trust powers under the Act;

(e) section 84, which describes the powers of a trust company, should be redrafted along the lines suggested in the Appendix to this report;

(f) sections 96 and 97 of the Act should be retained in their present form; and

(g) section 105 of the Act should be deleted.

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1. For a short summary of the law relating to savings and loan associations see "Handbook of Savings and Loan Law" prepared under the direction of The Committee on Savings and Loan Associations Section of Corporation, Banking and Business Law, American Bar Association, Chicago 1973.
2. The fixed interest rate controls may have contributed to the heavy withdrawals of funds from savings and loan associations during most of 1974. See article in the Wall Street Journal, September 20, 1974, p. 5. Recently there have been discussions in the U.S. concerning the "variable interest mortgage" which, if adopted by savings and loan associations would seem to require change in the existing controls over savings account interest rates.
3. At the London meetings the Committee heard from representatives of The Provincial Building Society of Bradford, Yorkshire. The Provincial is the seventh largest building society in England and, at December 31, 1973, had as many as 350,000 shareholders.
4. The Loan and Trust Corporations Amendment Act, 1970 (No. 2), S.O. 1970, c. 129, section 7.
5. See Report of the Registrar of Loan and Trust Corporations for the year ended December 31, 1972 at pages 14 and 19.

CHAPTER 7

Financial Intermediation

7.01 Financial intermediation is an important part of the business performed by loan and trust companies today. The term "financial intermediary" is understood by the Committee to mean the function that a financial institution serves when it acts as an intermediary between those with funds to lend and those wishing to borrow funds. The intermediary borrows the funds, paying interest to its lenders, and lends the funds to other parties, charging them interest on the loan. The difference between the income earned on investment of the funds (for example, the interest received on a mortgage) and the cost to the intermediary of the borrowed funds (for example, the interest paid to a customer on a savings account) represents the "spread" to the intermediary. The intermediary pays its expenses from the spread and any balance remaining represents its profit. It appeared to the Committee that loan corporations have always functioned primarily as intermediaries by borrowing funds from depositors and investors in their debentures and by lending the funds so received on mortgages. The Committee was advised that the character of a loan corporation's business has not changed significantly over the years, although there has been some shortening of the term on the borrowing side and some increase in the variety of debt instruments being sold.[1] The entry of trust companies into the field of financial intermediation has, by way of contrast and as already outlined in paragraphs 1.14 to 1.16, been comparatively recent. The brief submitted to the Committee by the Association (the "Association's brief") contains data for the period 1950 to 1973. The data shows that: (a) the growth of trust company intermediary business during the period 1950 to 1973 has been enormous; (b) the bulk of their intermediary funds has been reinvested in mortgages, mainly mortgages on residential properties; (c) trust companies and loan corporations now account for a major share of the mortgage loans made by private lenders to the residential market in Canada; and (d) for most companies, the bulk of their profits are derived from their intermediary business. During the period mentioned, intermediary assets of trust companies as a group increased from approximately $350 million in 1950 to approximately $10 billion in 1973.[2] By 1962, mortgages had become the principal asset in which intermediary funds were invested and by 1973 accounted for over 66⅔% of investments made with intermediary funds.[3] By the 1970's, loan and trust companies provided approximately 56% of all mortgage money loaned by private lenders to the residential housing market as compared with approximately 25% in the 1950's. It appeared obvious to the Committee, therefore, that financial

intermediation is a highly important part of the business of these companies, both from the standpoint of the companies themselves by contributing to their profits, and from the standpoint of the economy and consumer-public of Ontario.

7.02 Loan and trust companies have attracted these substantial accumulations of intermediary funds by taking deposits and by selling short term debt instruments, namely loan company debentures and trust company guaranteed investment receipts or certificates. While the Act draws a technical distinction between the deposits held by trust companies and those held by loan corporations and between the nature of the instruments they may sell to the public, for practical purposes the companies tend to look upon their intermediary funds in the same manner, that is, as moneys borrowed from the public for reinvestment by them as intermediaries. The Committee considered the desirability of retaining the distinctions in the Act. The main distinction is that loan corporations may borrow funds by taking deposits or selling debentures,[4] whereas trust companies, although prohibited from borrowing money by taking deposits or by issuing debentures,[5] may receive deposits as trustee for the depositor, may receive moneys for investment as trustee for the person lending the moneys, and may guarantee repayment of the moneys to such person plus interest at such rate as is agreed upon.[6] In law the relationship between the lender and a loan corporation is a debtor-creditor relationship, whereas the relationship between the lender and a trust company is a trustee-trust beneficiary relationship. Due to the existence of the trust relationship in the latter instance, the Act expressly provides that the trustee may retain the spread resulting from its intermediary operations and also provides for an ear-marking or setting aside of identified securities against all intermediary funds.[7] Technically speaking, therefore, the legal rights of the holder of a loan corporation debenture and the holder of a trust company receipt are not the same, although for practical purposes the Committee did not consider the differences to be significant. While there appears to be no adequate reason why trust companies should be prohibited from borrowing money by taking deposits or by issuing debentures, the Committee considers that confusion might arise if trust companies were permitted to receive intermediary funds on either a debtor-creditor or trustee-trust beneficiary basis at the companies' option. Trust company receipts and certificates appear to have gained acceptance in financial markets over the years on the basis of the trust concept, and the Committee is unaware of any compelling reason to change the practices that are well established today. The Committee received no submissions requesting that the distinctions in the Act be removed. The Association's brief argues in favour of their retention.[8] The Committee recommends therefore that the prohibition

in section 87 (1) of the Act to the effect that an Ontario trust company does not have power to borrow money by taking deposits or by issuing debentures, should be retained. Section 87 (1) was amended in 1974 to make it possible for Ontario trust companies, subject to the regulations, to borrow money by the issue of subordinated notes. The Committee concurs with the general principle of this amendment but, as indicated in paragraph 7.04, refrains from making any specific recommendations thereon since there has not yet been an opportunity to observe the principle in operation.

7.03 The intermediary powers of loan and trust companies are subjected to a number of statutory controls under the Act. These controls are (a) the requirement that a by-law must be passed and filed with the Registrar before the intermediary powers may be exercised;[9] (b) the imposition of a statutory limit on the total intermediary borrowings of a company at any one time;[10] and (c) the requirement to maintain a liquidity reserve against intermediary borrowings.[11] The first two controls will be discussed further in this paragraph. Liquidity is dealt with in Chapter 8. The objective of the first two controls appeared to the Committee to be protection of the shareholders, depositors, and holders of debentures and receipts against excessive borrowings by the company. Prior to the 1974 amendments, the basic control provided that the total amount borrowed by a registered company as an intermediary "shall not at any time exceed an amount equal to four times the aggregate of its unimpaired capital and reserve".[12] The Lieutenant Governor in Council was then given a discretionary power to increase the four times multiple to a maximum of 20 times on application by the company for the increase, on report of the Registrar, and on such terms and conditions as are prescribed in the order in council.[13] Since it is the practice to require a company to state the multiple applicable to it in its borrowing by-law, the company's application for an increase in multiple has to be supported by a new by-law containing the proposed multiple. Prior director and shareholder approval of the increase is thereby ensured. Substantially similar provisions are contained in the Federal Acts and the Acts of the other provinces. The Committee found, however, that the approach is not always adopted for financial institutions. For example, the Committee was advised during its hearings in London that The Protection of Depositors Act, 1963, which was adopted to regulate the activities of so-called "fringe banks" in Britain, simply controlled the advertisements of these institutions and did not impose a statutory maximum upon their borrowings.[14] The Committee was of the view that the approach taken by the Act was preferable to the British approach. The Committee was advised by those responsible for the Act's administration that registered companies are customarily required to apply for

several orders in council before reaching the maximum multiple of 20 times. New companies would be started out at the statutory minimum and increased by stages to higher levels. Indications were given to the Committee during its hearings that a number of companies had reached or were about to reach the statutory maximum, and towards the end of its hearings in December, 1974, a bill was introduced in the Ontario Legislature. Under the bill, which is now law, extensive changes were made to the sections of the Act which limit the amount of intermediary borrowings. The minimum multiple for trust companies was increased to 12.5 times to conform with the existing minimum for federal trust companies under the Trust Companies Act;[15] provision is made for the issue of "subordinated notes"; and companies which meet a standard of financial condition to be prescribed by regulation may be permitted to increase their intermediary borrowings above the 20 times maximum. These changes generally follow those of the amendments to the Federal Acts previously introduced although there are differences in detail between the federal and Ontario approaches.[16]

7.04 The Committee considers that it would be inadvisable for it to comment in detail on these new statutory provisions. Owing to their recent introduction, the Committee had insufficient time to review the provisions in depth and, at the time of writing this report, regulations as contemplated by the Ontario amendments have not been issued. The Committee supports, however, the general principles of these amendments which the Committee understands are designed to increase the "borrowing" capacity of registered companies as intermediaries. The Committee concurs with the retention of a statutory discretion in this area of the Act. In the Committee's opinion, the existing provisions for an authorizing by-law, review by the Registrar, and grant of any increase in intermediary powers by order in council should be retained in the interests of providing protection to the shareholders, depositors, and holders of securities of these institutions.

7.05 Additional protection to depositors and holders of debentures and receipts of registered loan and trust corporations is provided by deposit insurance. In 1967, the Ontario Legislature created the Ontario Deposit Insurance Corporation for the purpose of providing deposit insurance to loan and trust companies carrying on business in Ontario.[17] The new legislation was not implemented, however, and by arrangement with the federal authorities, Ontario corporations were permitted to become members of the Canada Deposit Insurance Corporation (hereinafter referred to as the "CDIC").[18] Members may obtain a policy of deposit insurance whereby CDIC insures "deposits" received or held by the member to a maximum of $20,000 of the unpaid balance of the aggregate moneys received from, or held to the credit of, any one depositor. Annual premiums

for the insurance are paid to CDIC by the member. The Committee was advised by the Registrar that no registered corporation may act as an intermediary in Ontario unless it holds a deposit insurance policy issued by CDIC. The Committee considered the question of whether the existing coverage of $20,000 was adequate in view of the fact that it has remained unchanged since it was first fixed in 1967. A submission was received from the Association to the effect that the existing premiums were too high for the amount of coverage provided and that the coverage could be increased while retaining the same premium payable.[19] The Committee also understands that during 1974, the coverage afforded to depositors in banks insured by the Federal Deposit Insurance Corporation of the United States was increased from $20,000 to $40,000. In the Committee's opinion, there should be an increase in the amount of coverage provided to the depositors in Ontario of loan and trust corporations. The Committee recommends that the amount be $40,000 for any one 'deposit' and recommends that the Government of Ontario initiate discussions with the federal authorities to secure such additional coverage for Ontario members of CDIC. It appeared to the Committee that the loss experience of CDIC has been such that the proposed increase in coverage should require little, if any, increase in premium.

7.06 The Committee understands that considerable research has been carried out in Canada, principally by the banks, concerning the possibility of establishing an electronic payment system whereby funds would be transferred by computer entry instead of by cheque. While this subject would appear to take the Committee beyond its terms of reference, the Committee makes reference to it because the topic was raised on a number of occasions during its hearings and is of great importance to loan and trust companies as intermediaries. The Association's brief states[20] as follows:

> "The Association feels that access to an electronic payment system will be vital to the continued existence of trust companies as deposit-taking institutions. The advantages of such a system in terms of speed, convenience and flexibility will make it almost impossible to compete effectively without access to the system."

In the Committee's opinion, the intermediary activities of loan and trust corporations provide an important and desirable service to the residents of Ontario. The Committee notes that certain of these corporations are incorporated under Ontario law and observes that it would be a matter of concern to the Committee should loan and trust corporations cease to function as deposit-taking institutions by reason of their inability to gain access to an electronic payment system available to other financial institutions in Ontario. The Committee therefore recommends that the

Government of Ontario should encourage the establishment of a common user form of electronic payment system and should support the entry of Ontario corporations, on a fee-for-service basis, into the system, on condition that Ontario corporations entering the system remain under provincial regulation and control and that such a system is acceptable to the Government of Ontario. The Committee also considers that the Government of Ontario should make its views in this regard known to the Government of Canada, which, the Committee understands, is actively following developments in this area.

7.07 The Committee understands that trust companies have in recent years sold income averaging annuity contracts to individuals. The purpose of such a contract is to enable an individual to spread unusually large income receipts over a number of taxation years in order to reduce the total amount of income tax payable. The individual makes a lump sum payment to the trust company in return for the company's contractual commitment to pay to the individual an agreed monthly or yearly sum for an agreed period of time. The duration of the contract can be for as long as 15 years if the individual's age is 70 years or less at the time the contract is made. The Committee understands that section 89 of the Act, which deals with the receipt of moneys for guaranteed investment, is interpreted by the industry and by the Registrar and his staff as conferring upon registered trust companies the necessary authority to sell income averaging annuity contracts. While these contracts are analogous to guaranteed receipts or certificates, they normally provide for payments over a longer period of time and at more frequent intervals. Performance of the contracts would seem to involve the companies in additional work for which they should in the Committee's opinion, be entitled to make a reasonable charge in addition to any profits earned through investment of the moneys received at the time of the purchase of the contract. The Committee has concluded that the Act should expressly provide for the sale by registered trust companies of income averaging annuity contracts and therefore recommends that section 89 of the Act be amended accordingly. The Committee would add the qualification that any such contract sold by a trust company should not provide that the payments to be made thereunder are conditional upon the continued life of the annuitant during the term of the contract.

7.08 **The Committee recommends that:**

(a) the prohibition in section 87 (1) of the Act to the effect that an Ontario trust company does not have power to borrow money by taking deposits or by issuing debentures should be retained, subject to the qualification that Ontario trust companies should have power to borrow money by the issue of subordinated notes in accordance

with section 87 (1) as amended in 1974;

(b) the statutory discretion with respect to the extent of the exercise of intermediary powers by loan and trust corporations should be retained;

(c) the Government of Ontario should approach the federal authorities with a view to obtaining an increase in the coverage afforded by deposit insurance from $20,000 to $40,000 of the unpaid balance of the aggregate moneys received from, or held to the credit of, any one depositor, such increase to be granted with little, if any, increase in premium, in view of the Committee's findings as expressed in paragraph 7.05;

(d) the Government of Ontario should encourage the establishment of a common user form of electronic payment system; should support the entry of Ontario corporations, on a fee-for-service basis, into such a system instituted in Ontario, on condition that Ontario corporations entering the system remain under provincial regulation and control; and should make its views in this connection known to the Federal Government; and

(e) section 89 of the Act should be amended to provide expressly for the sale by trust companies of income averaging annuity contracts.

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1. Submission of The Trust Companies Association of Canada to the Select Committee on Company Law of the Ontario Legislative Assembly, dated December 1974, at p. 11. The submission is referred to henceforth in the report as the "Association's brief".
2. Association's brief, chart 5 p. 10B.
3. Association's brief, p. 11.
4. The Act, section 78 (2). Before a loan corporation may exercise its powers, however, a by-law must be passed in accordance with section 78 (3).
5. The Act, section 87 (1). This prohibition applies to Ontario trust companies only. Federal and extra-provincial companies are placed under a similar prohibition by their own Acts.
6. The Act, sections 88 and 89.
7. The Act, sections 88 and 89.
8. Association's brief, p. 35.
9. The Act, sections 78 and 89a.
10. The Act, sections 82 and 90.
11. The Act, sections 81 and 93.
12. The Act, sections 82 and 90.
13. The Act, sections 82 and 90.
14. Protection of Depositors Act, 1963, Statutes of the United Kingdom, Eliz. 2, c. 16.
15. Trust Companies Act, R.S.C. 1970, c. T-16, section 70 (3).
16. Bill S-7, an Act to authorize federal trust companies and loan companies to increase the monetary limit of their borrowing power and to issue subordinated notes. Assented to November 27, 1974, S.C. 1974-75, c. 7.
17. The Ontario Deposit Insurance Corporation Act, 1967, S.O. 1967, c. 61.
18. CDIC was created by the Canada Deposit Insurance Corporation Act, S.C. 1966-67, c. 70.
19. Association's brief, p. 73.
20. Association's brief, p. 71.

CHAPTER 8

Liquidity

8.01 The Act requires each registered corporation to maintain a liquidity reserve against intermediary funds of the corporation repayable on demand or in less than 100 days. Section 93 provides:

> "93 (1) Every registered trust company shall at all times maintain,
>
> (a) cash on hand or on deposit in a chartered bank or other depository approved by the Registrar;
>
> (b) unencumbered debentures, bonds, stocks or other securities of or guaranteed by the Government of Canada or of or guaranteed by any province of Canada;
>
> (c) loans payable on demand and fully secured by securities referred to in clause b; and
>
> (d) subject to the approval of the Registrar and to such conditions as the Registrar may impose, a credit from chartered banks in Canada,
>
> to an aggregate of at least 20 per cent of the amount of deposits and of funds received for guaranteed investment coming due in less than 100 days.
>
> (2) Of the amount maintained under clauses a, b and c of subsection 1,
>
> (a) at least 25 per cent shall be maintained in cash on hand or on deposit in a chartered bank or other depository approved by the Registrar and in unencumbered debentures, bonds, stocks or other securities of or guaranteed by the Government of Canada, maturing in three years or less; and
>
> (b) at least 50 per cent shall be maintained in cash on hand or on deposit in a chartered bank or other depository approved by the Registrar and in unencumbered debentures, bonds, stocks or other securities of or guaranteed by the Government of Canada, maturing in ten years or less."

Substantially the same requirement applies to registered loan corporations under section 81 of the Act. These provisions of the Act require registered corporations to maintain a portion of their intermediary funds in liquid form, ordinarily in the form of cash on hand or on deposit in a chartered bank or unencumbered debt obligations of or guaranteed by the Government of Canada. The approach followed by the Act is

to authorize a reasonably broad list of permitted investments for the entire reserve, including cash, debt obligations of or guaranteed by the Government of Canada or any province of Canada, demand loans fully secured by such securities, and, subject to the approval of the Registrar, bank lines of credit.[1] The list is then cut down by subsection (2) of sections 81 and 93 which provides, in effect, that 50% of the reserve must be maintained in highly liquid securities, that is, in cash and debt obligations of or guaranteed by the Government of Canada maturing in ten years or less, subject to the further requirement that at least 25% of such highly liquid reserve must be maintained in cash and debt obligations of or guaranteed by the Government of Canada maturing in *three* years or less.

8.02 The Committee agrees with the principle that corporations registered under the Act should be required to maintain liquid reserves against intermediary funds repayable on demand or in less than 100 days. The Committee considers, however, that some amendments should be made to the existing requirements. The Committee was advised by the Association that many companies maintain a cushion of additional liquidity above the 20% statutory minimum. The cushion is maintained to guard against any possible temporary infringement of the statutory minimum and not from any conscious decision by management of the company concerned that a higher reserve is necessary for business reasons. Representatives of the Association and of the industry advised the Committee that in their view, the statutory minimums were too high and inhibited their ability to make maximum use of intermediary funds for reinvestment, including investment in residential mortgages. The Association's brief contained a lengthy submission on the subject of liquidity.[2] It was argued that the existing levels are too high and that loan and trust companies were at a competitive disadvantage to some other financial institutions, in particular the banks, that are permitted to operate at lower levels. It was also argued that changes in the composition of the reserve should be made in view of the greater variety of liquid short-term instruments available today in financial markets. The Committee concurs with certain of the submissions of the Association and recommends the following changes:

(a) the liquidity reserve in sections 81 and 93 of the Act should be reduced from 20% to 15%;

(b) the distinction between a liquid reserve made up of the cash, securities and credit lines listed in sections 81 (1) and 93 (1) and the highly liquid reserve called for by sections 81 (2) and 93 (2) should be removed and henceforth the liquid reserve should be composed entirely of:

(i) cash on hand or on deposit in a chartered bank or other depository approved by the Registrar, provided that such funds are in Canadian or U.S. dollars;

(ii) unencumbered debentures, bonds, stocks or other securities of or guaranteed by the Government of Canada, or the Province of Ontario, or, subject to the approval of the Registrar, any other province of Canada, maturing in three years or less;

(iii) subject to the approval of the Registrar and to such conditions as the Registrar may impose, a credit from chartered banks in Canada; and

(iv) commercial paper subject to the following special requirements:

1. the issuer must be on a list approved by the Registrar;
2. the commercial paper should mature in less than 100 days from the date that it is acquired by the registered company; and
3. when originally issued, the commercial paper must be for a term of one year or less; and

(c) registered companies should no longer be required to maintain liquidity on a daily basis but should be permitted to average their demand liabilities and liabilities due in less than 100 days on a monthly basis and should be deemed to be in compliance with the liquidity reserve requirements if 15% of the average of such liabilities during the preceding month is maintained throughout the current month.

The Committee understands that the averaging principle set forth in recommendation (c) above is substantially the same as the principle used by the chartered banks in calculating their liquidity reserves under the Bank Act.[3] The Committee does not consider that secured dealer call loans should be included within the liquidity reserve as recommended in the Association's brief.

8.03 The Committee understands that Government of Canada deposits with the chartered banks help to compensate the banks for outflows of deposit funds arising from Canada Savings Bond sales and tax payments. It also understands that loan and trust companies suffer seasonal outflows for the same reasons but do not enjoy the compensating advantage of being permitted to receive Government deposits. In the opinion of the Committee, the intermediary role of loan and trust companies in Ontario would be strengthened if registered companies were eligible to receive Government deposits as part of their intermediary funds. The Committee therefore recommends that section 11 (2) of The Financial Administration Act[4] be amended so as to include registered loan and trust companies

as depositories that may be designated by the Treasurer of Ontario for the deposit of public money pursuant to that section.

8.04 The Committee noted that it is not entirely clear whether the phrase "coming due in less than 100 days" at the end of section 93 (1) modifies "deposits" as well as "funds received for guaranteed investment". The Committee understands that in practice, section 93 (1) is interpreted so that the phrase does modify both terms. The Committee therefore recommends that the concluding part of subsection (1) of section 93 be changed to read:

> "to an aggregate of at least 15 per cent of the amount of deposits repayable on demand or coming due in less than 100 days and of funds received for guaranteed investment repayable on demand or coming due in less than 100 days."

The Committee also recommends that a corresponding change be made to section 81 (1).

8.05 **The Committee recommends that:**

(a) the liquidity reserve in sections 81 and 93 be reduced from 20% to 15% of the demand or maturing obligations due within 100 days;

(b) 100% of the liquid reserve required to be maintained under sections 81 and 93 should be composed of the following assets:

  (i) cash on hand or on deposit;

  (ii) obligations of or guaranteed by the Government of Canada, the Province of Ontario or, subject to the approval of the Registrar, any other province of Canada, maturing within three years or less;

  (iii) bank lines of credit that are approved by the Registrar; or

  (iv) commercial paper if, 1. the issuer is approved by the Registrar; 2. the commercial paper will mature in less than 100 days; and 3. the commercial paper when originally issued was for a term of one year or less;

(c) a company should be considered to be in compliance with the 15% liquid reserve requirement if during a month, it maintains a reserve equal to 15% of the average of its demand and maturing obligations due within 100 days during the preceding month;

(d) dealer call loans should not be permitted to be included in the liquid reserve;

(e) section 11 (2) of The Financial Administration Act (Ontario) be amended so as to permit designation of registered loan and trust companies as depositories for public money; and

that the liquid reserve must be maintained against (i) all deposits repayable on demand or within less than 100 days; and (ii) obligations or funds received for guaranteed investment, as the case may be, payable on demand or coming due in less than 100 days.

1. The Act, sections 81 (1) and 93 (1).
2. Association's brief, pp. 35-36 and Exhibit "A" thereto.
3. Bank Act, R.S.C. 1970, c. B-1.
4. The Financial Administration Act, R.S.O. 1970, c. 166, section 11 (2); 1971, Vol. 2, c. 55; 1971, (2nd Sess.), c. 12; 1972, c. 1; 1973, c. 142; 1974, c. 15.

CHAPTER 9

Administration Of Estates And Trusts

9.01 As described in Chapter 1 above, the traditional role of the trust company has been to provide fiduciary services, primarily in the administration and trusteeship of the estates of deceased persons, the estates of minors and mental incompetents, and in caring for assets given by living individuals to be held in trust (generally termed "inter-vivos trusts"). The Committee considers that this fiduciary role remains the hall-mark of the trust company today, as reflected in the definition of trust company found in section 1 (p) of the Act: " 'trust company' means a company constituted or operated for the purpose of acting as trustee, bailee, agent, executor, administrator, receiver, liquidator, assignee, guardian of a minor's estate, or committee of a mentally incompetent person's estate." Chapter 1 has shown how trust companies have entered into new areas of activity, including that other major trust company activity — financial intermediation in its varied aspects.

9.02 Evidence before the Committee indicated that, as the profitability of this latter field became more apparent, the trust industry has tended to stress financial intermediation as an area of activity. As a result, while the more traditional fields of executorship and trusteeship have continued to grow on an industry-wide basis, they may, to some extent, have been overshadowed. This trend has been of concern to the Committee throughout its extended hearings and was a constantly recurring theme. It must not be inferred that the companies in the industry have in any way abdicated their function as executors and personal trustees, indeed their submissions expressed a similar concern. Those trust companies that have become sufficiently well established to have built up a portfolio of substantial estates appear to be fulfilling their responsibilities in a manner that is consistent with the high responsibilities that are imposed on corporate trustees by the law of trusts.

9.03 In the Committee's opinion there has been some decline in the interest of the industry in executorship activities, particularly in the case of small and average-sized estates, that is to say, estates with assets to a value of $150,000 or less. Some companies consider that it is not desirable to administer estates of a value under $60,000 while other companies prefer not to accept the administration of estates with a value under $150,000. The Committee was advised that the reason for a declining interest in the administration of small and average-sized estates by trust companies is that estate administration has become a relatively low-profit activity and when viewed from the over-all activities of a trust

company, appears relatively uneconomic. While no specific financial data was given, estimates made by the Association in its brief to the Committee indicated that, with one exception, approximately 25% of the profits of the large companies comes from their fiduciary business, with 75% coming from their intermediary business.[1] It was roughly estimated that, in relation to assets employed in the business, the rate of return from the fiduciary business was only approximately one-fifth of the return from the intermediary business.[2] It is reasonable to infer that the former activities are even less profitable in the case of small trust companies that are unable to enjoy the economies of estate administration on a large scale. It is significant that trust company officers, whom the Committee interviewed in detail both in New York City and in the United Kingdom, corroborated the Trust Companies Association's statement as to the unprofitability of small estate administration. Indeed some American trust officers indicated that the administration of estates was profitable to their companies only to the extent that it provided funds for short-term deposit in the commercial departments of the banks concerned.

9.04 There appear to be several factors that contribute to the unprofitability of small estate administration. First, the administration of estates is highly labour intensive: the personnel that it requires must be well-trained and thoroughly experienced, and high staff costs are the inevitable result. Second, the complexity of estate administration has escalated over the years as the law has become increasingly complicated and the costs of administration have increased correspondingly. On the other hand, these increasing costs have not been matched by corresponding increases in compensation. The Committee was advised that compensation to corporate trustees is not based on a graduated percentage scale and that fee levels to corporate trustees have not changed to any significant degree in Ontario for many years. While asset values have increased due to inflation there has been to some extent a fragmentation of the assets in the typical family estate. Frequently such assets consist of jointly-owned real and personal property, life insurance and pension plans, all of which pass or are payable directly to the survivors or to named beneficiaries independently of the testator's will. Since such assets are not treated as a part of the estate when compensation is being calculated, the base of the executor's remuneration has been increasingly eroded. Discussions before the Committee indicated that the nature of the scheme of distribution of the typical estate has also been changing over the years. More estates are being planned for immediate distribution and fewer estates are planned for long-term trust management. The latter type of estate is the one where corporate trustee services are often most needed. Such a trend will no doubt result in declining revenues from long-term

financial management, which is the very aspect of estate administration that has traditionally been most profitable to the trust companies.

9.05 The Committee is concerned by the trend away from estate administration by corporate trustees, particularly in the case of the small and average-sized estates. The Committee is of the opinion that there is a constant need in Ontario for the services of corporate trustees in the field of estate administration for those estates, whether large or small, where there are continuing trusts requiring the varied services provided by the professional corporate trustee. In particular, the financial services provided by corporate trustees are needed and should be more available to small and average-sized estates especially in the areas of estate planning, estate management and long-term investment of estate assets. While individual trustees, such as lawyers, accountants and others, have traditionally played a significant part in the carrying out of these responsibilities and can be expected to continue to do so, the corporate trustee enjoys the advantage of perpetual existence and a wide variety of professional talents at its disposal. The Committee has therefore concluded that it is important and urgent that steps should be taken to ensure that the trust companies will continue to emphasize estate administration for all estates as an important part of their business activities.

9.06 The Committee accordingly recommends the immediate establishment of an appropriate group such as a committee of the Legislative Assembly to make an intensive study of the law of the administration of estates and of the practice and procedure that surrounds that field of law, with a view to recommending changes that would reduce the cost of performing such fiduciary services, and that would rationalize the method of calculating the compensation that should be chargeable for such services. Since this Committee's terms of reference are limited to reporting upon specialized types of companies such as trust companies, it would be inappropriate for the Committee to make any specific recommendations regarding changes in the general law and procedure of estate administration. It would nevertheless appear appropriate for the Committee to itemize some of the topics that, as appeared from the evidence before the Committee, merit further consideration by the proposed new committee. Such topics are:

(a) a study of the kinds of services that should be available from trust companies for the planning, administration and management of small and average-sized estates;

(b) a study of the role of the Public Trustee;

(c) a review of the Surrogate Court procedures leading to the grant of letters probate and letters of administration, with a view to a simplification of the procedures and of the necessary documentation;

(d) a review of the procedures required under the Ontario Succession Duty Act in order to determine (i) whether they can be further simplified; and (ii) whether they can be co-ordinated with Surrogate Court procedures and documentation so as to minimize duplication;

(e) a consideration of the types and values of assets that personal representatives should be permitted to dispose of without being required to obtain succession duty releases and without being required to obtain letters probate or letters of administration. (Sections 170 and 171 of The Loan and Trust Corporations Act now make provision for the prompt and inexpensive disposition of small deposits, debentures, and guaranteed investment certificates with a minimum of formality and the proposed new committee might wish to consider further application of the principles upon which those sections are based.);

(f) a review of the law as to the transmission of securities out of the name of the deceased with a view to simplifying the requirements that must be fulfilled in order to transfer ownership to the executor or a purchaser or to the beneficiary. (The proposed new committee might wish to consider the desirability of recommending the enactment of uniform legislation on this topic in all Canadian jurisdictions.);

(g) a study of the procedures and documentary requirements that must be fulfilled in order to obtain payment of the proceeds of life insurance policies and pension plans. (The proposed new committee might wish to consider the enactment of legislation providing for uniform proof-of-claim documents for all life insurance companies and pension plans.);

(h) This Committee observed during its investigations in the United Kingdom that agreements between a corporate trustee and a testator made during the testator's lifetime, providing for the compensation to be payable to the trustee in accordance with its scale of fees in force at the date of the testator's death, were given full force and effect by the courts. (The proposed new committee might wish to consider the adoption of such a system in this jurisdiction although this Committee, in making reference to the use of these agreements in the United Kingdom, does not intend to imply that it either approves or disapproves the practice.); and

(i) a review of the law relating to the compensation payable to executors and trustees, including study of the question whether executors and trustees should be permitted to take "progress draws" out of the estate assets on account of their compensation as work on the estate

administration proceeds. In recommending changes, the proposed group or committee should give appropriate weight to any savings or additional compensation that might accrue to a registered trust company as a result of the implementation of the Committee's recommendations in paragraphs 9.07, 11.02 and 11.04.

9.07 The Committee received a submission from the Association to the effect that trust companies should be permitted to deposit uninvested funds from the capital and revenue accounts of estate and trust accounts under their administration in their own savings departments. As the Ontario law now stands, trust companies are precluded from depositing funds in such manner by the rule of trust law to the effect that a trustee must not let his interest conflict with his duty. Trust companies have therefore followed the practice of depositing such funds with other entities such as the chartered banks. In view of the temporary nature of these deposits, the Committee is of the opinion that there should be some relaxation of the trust law principles insofar as they apply to trust companies in this connection. The Committee therefore recommends that a new section be added to the Act authorizing registered trust companies to deposit uninvested funds from the capital and revenue accounts of estate and trust accounts of which they are a fiduciary in their own savings departments. The section should provide that the trust company is to be entitled to retain any interest or profit resulting from the investment or loaning of such deposit money in excess of the amount of interest payable to the individual estate or trust concerned. The Committee would observe that trust companies exercising such a new power should use it with circumspection so that amounts invested from time to time with the savings department from any individual estate or trust should not be permitted to increase to unreasonable levels and should be placed in more permanent investments as promptly as possible in order for the trustee to discharge its duties as executor and trustee.

9.08 A second submission received from the Association concerned a requested change in the Act to permit a trust company to invest funds held for different estates and trusts in its own guaranteed investment certificates or receipts. This matter was considered by the Committee which has concluded that no change in this connection should be made. The Committee believes that to change the law in this respect would considerably erode the equitable principle that a trustee must not let his interest conflict with his duty. In the Committee's view, it is undesirable to make such a significant exception to this important and well-understood rule of equity.

9.09 **The Committee recommends that:**

(a) an appropriate group such as a committee of the Legislative

Assembly be established to make an intensive study of the law of the administration of estates and of the practice and procedure that surrounds that field of law with a view to recommending changes that would reduce the cost of performing such fiduciary services and that would rationalize the method of calculating the compensation that should be chargeable for such services to the end that the specialized services and skills of corporate trustees would be broadly available (suggested matters for consideration by such a committee are outlined in paragraph 9.06);

(b) the Act should be amended to permit registered trust companies to deposit uninvested funds from the capital and revenue accounts of estates and trusts of which they are the trustee in their own savings departments and should provide that the company so depositing funds is entitled to retain the interest and profit from the investment or loaning of such deposit money in excess of the amount of interest payable to the estate or trust concerned; and

(c) that there be no change made in the Act to permit a registered trust company to invest the funds of estates and trusts under its administration in its own guaranteed investment certificates or receipts.

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1. Association's brief, p. 18.
2. Association's brief, p. 18.

CHAPTER 10

Investment Powers

10.01 The investment powers of loan and trust companies are controlled in a variety of ways under the Act. These controls affect the companies' freedom to deal with their own funds, that is their paid-in capital and retained earnings, and their intermediary funds. The Act does not appear to deal with the investment of estate, trust and agency funds because the investment powers of a corporation in respect of these funds are established outside the Act by the terms of the relevant agreement or will itself and, in some circumstances, by the investment sections of the Trustee Act.[1] This Chapter then, deals with investment powers only insofar as they apply to company funds and intermediary funds. In referring to "investment powers", the Committee intends to cover both meanings of the term, that is a company's power to purchase a security as an investment and its power to lend funds on a security, without drawing a distinction between the two meanings as the Act does in sections 150 and 153.

10.02 The basic approach taken by the Act is to specify a detailed list of "authorized investments" in which a registered corporation may invest funds. Section 150 (1) gives the list for a loan corporation and enumerates 16 different types of investment. The list is carried through for trust companies in section 153 (1). The list contains restrictions which relate to the quality of the investments, that is requirements as to the financial strength of the entity that has issued them. If a security does not fall within the list, then ordinarily and subject to some exceptions, a registered corporation may not invest in it. The exceptions are of course, the power conferred by sections 151 and 154 to make unauthorized investments within the so-called "basket" of the corporation and the power to invest company funds in the shares of associated or subsidiary companies under sections 152 and 155. The basket provisions impose an upper limit on the total book value of investments that may be included within the basket. The maximum limit is, for practical purposes, an amount not exceeding 7% of the book value of the total assets of a loan corporation or, in the case of a trust company, 7% of the aggregate of the unimpaired capital and reserve of the company and the intermediary funds of the company.[2] The Registrar is given a statutory discretion to fix the actual percentage available to each individual company.[3] Using these basket provisions, companies have limited ability to make consumer and commercial loans which are not authorized investments under the Act. The regulations issued under sections 152 and 155 also

impose restrictions upon investments of company funds in the shares of associated or subsidiary companies.[4] Having specified a list of authorized investments, the Act superimposes additional restrictions as to quantum in section 157 and expressly prohibits certain other investments under section 163, such as loans to directors and investments in the securities of companies that are linked to the registered corporation. The Committee understands that the approach taken by the Act to investment powers is substantially similar to the approach followed by the Federal Acts and to that followed by the acts of most of the other provinces.

10.03 The Committee was of the opinion that in view of the highly technical nature of the investment powers sections and of the considerable uniformity that exists between them and the comparable sections of the Federal Acts and the acts of the other provinces, it would serve no useful purpose for the Committee to review the detail in sections 150 (1) and 153. The Committee asked the Registrar to comment with respect to the detailed list in sections 150 (1) and 153 (1) and to advise whether, in his view, the list was generally satisfactory today, both to the industry and to the Registrar. The Registrar advised[5] that the lists have generally proven to be adequate and drew to the Committee's attention two recommended changes. The first concerns section 150 (1) (j) which deals with investment in obligations or certificates issued by a trustee to finance the purchase of transportation equipment to be used on railways or public highways. Some companies have made investments on the security of airplanes and these investments have had to be placed in the basket. The Committee agrees that the scope of section 150 (1) (j) should be broadened and recommends that the phrase "to be used on railways or public highways" be deleted.

10.04 The second change was that the phrase "improved real estate" where used in section 150 (1) (a) of the Act be defined. The Committee interprets this recommendation to extend not only to section 150 (1) (a) but throughout sections 150 and 153 where the expression is used. The word "improved" was added to the Act when it was revised in 1949,[6] but no definition of "improved real estate" was attemped in the revised Act. Differences of opinion as to the meaning of "improved real estate" between the Registrar and companies registered under the Act have arisen from time to time.[7] The Committee was advised that it is the present policy of the Registrar and his staff to interpret the phrase to mean (a) vacant land that has been subdivided pursuant to a registered plan of subdivision and is fully serviced; and (b) agricultural land on which actual farming or ranching operations are being conducted. In the case of agricultural land, the Registrar requires it to be valued for mortgage purposes at its agricultural value and not otherwise. The Committee was referred to the definition of improved real estate in the Alberta Act[8] but considers it to be too restrictive since it appears to require that mort-

gage funds must be advanced to pay for building construction on the real estate and not in payment for services already in place. The Committee recommends that a definition of improved real estate be added to the Act based on the interpretation given to the phrase by the Registrar as mentioned in this paragraph 10.04. The Committee recommends, however, that the present policy be relaxed somewhat by removing the requirement that the real estate must be fully serviced. The Committee recommends that the principle in section 4 (k) of The Land Speculation Tax Act, 1974[9] should be followed so that the real estate would be considered "improved" if it is wholly or partly serviced to the extent that construction of a building on the real estate could lawfully be commenced, and, where applicable, to the further extent that a permit authorized by a by-law passed pursuant to subsection 1 of section 38 of The Planning Act by the municipality within which the real estate is situated, or a permit authorized by section 17 of The Public Lands Act, would be available.[10]

10.05 The Association's brief contained a submission in favour of a change in the basic approach of the Act to investment powers as well as some requested specific amendments. With respect to a change in the basic approach, the Association submitted that companies should be permitted to make any investment that is not prohibited by the Act. Such an approach would follow that of the Bank Act[11] in its treatment of the investment powers of the chartered banks. In the Committee's opinion, the existing approach in the Act to investment powers, with its emphasis on the quality of an investment, should be retained. The Committee considers that there would be very little to be gained in adopting the new approach as proposed since, in the Committee's view, most of the existing provisions would have to be retained and recast as prohibitions thereby producing a long list of prohibitions. In addition, new prohibitions might have to be added from time to time to meet changing investment practices in financial markets. The discussion of this matter, however, caused the Committee to re-examine the "basket" provisions of the Act. The Committee was advised that most companies enjoying the upper limit of 7% in their basket do not make use of it to the maximum extent possible and most companies rarely go above 4%. It would appear that greater use could be made of the basket which could be used as a stepping stone for adding new categories of investment to the authorized list. For example, investments on the security of airplanes, which are now included in the basket, have been recommended for addition to the authorized list. The Committee considered but rejected, on the other hand, the request of the Association that consumer loans be added to the authorized list. The Committee is aware that companies often preserve unused capacity in the basket so that unqualified investments that are acquired inadver-

tently may be retained. This would partially explain why companies do not fully use their baskets. In order to encourage use of the basket as a stepping stone and to give companies some added flexibility, the Committee recommends that the upper limit for the basket be increased from 7% to 10% of the book value of a loan corporation's assets or of a trust company's unimpaired capital and reserve and intermediary funds, as the case may be. The Registrar should retain his statutory discretion to fix the actual percentage for each company within the proposed new maximum limit.

10.06 The Association's brief requested that section 157 (1) (b) be amended so as to permit an investment in more than 20% of the shares of a company subject to an appropriate limitation on the percentage of the registered corporation's assets that may be so invested.[12] The Committee notes that under the Act as it now stands, corporations may be permitted to acquire more than 20% of the shares of certain specialized companies included within the categories in sections 152 and 155. If authorized by the Lieutenant Governor in Council, power is also conferred on a loan corporation to acquire more than 20% of the shares of another loan corporation under section 115 as a preliminary to a joining together of the businesses of both corporations. A somewhat wider power is conferred on trust companies under section 117. The Committee considers that, outside the exceptional cases just mentioned, it is undesirable to permit registered corporations to acquire more than 20% of the stock of another corporation. Moreover, to permit this would appear to the Committee to be in conflict with the principle behind sections 152 and 155. Accordingly, the Committee recommends that no change be made in section 157 (1) (b).

10.07 The Committee received submissions to the effect that section 157 (1) (a) was too restrictive insofar as mortgage lending is concerned. Section 157 (1) (a) limits the amount of a company's own funds and its intermediary funds that may be invested in any one security or in the securities of one bank or company or group of associated companies. Where the investment is in a number of securities of the same issuer, a distinction is drawn between securities which mature in more than one year and those which mature in one year or less. In the latter case, a higher dollar limit is available. The Committee understands that the purpose of the section is to prohibit companies from investing too heavily in one security or in the securities of a single company or group of companies. The Committee considers that this is a desirable statutory safeguard and that it should be retained. The Committee is of the opinion, however, that some relaxation in the mortgage lending field is desirable. It was noted that "securities issued or guaranteed by the Government of Canada or the government of any province of Canada or by any municipal

corporation in Ontario" are excepted from the restrictions in section 157 (1) (a): an exception that would include NHA mortgages. The submissions to the Committee pointed out, however, that government guaranteed mortgage loans are ordinarily subject to maximum limits per residential property and that with rapidly increasing land and construction costs, there has been an increasing need for conventional mortgage loans, which are not subject to statutory maximum loan limits, and contain provision whereby repayment of the excess of the loan above 75% of loan value is insured by a private insurer. A conventional loan of this type is an authorized loan under sections 150 (3) (d) and 153 (4) (d) of the Act but is not included in the exception in section 157 (1) (a). Consequently, companies making a number of these conventional loans to a subdivision owner or a large conventional loan to an apartment building owner, have found themselves constrained by the restrictions in section 157. The Committee believes that it would assist the flow of mortgage funds to the residential housing market if the exception were broadened to include such conventional mortgages. Accordingly, the Committee recommends that investments made by registered companies under sections 150 (1) (c), 150 (3) (d), 153 (1) and 153 (4) (d) of the Act in mortgages for residential purposes be excluded from the restrictions in section 157 (1) (a) of the Act.

10.08 The Committee notes that section 157 in referring to investments made in any one company also specifically uses the word "bank". Section 150 (1) on the other hand, only refers to "company" although the Committee understands that "company" in that context is interpreted by those responsible for administration of the Act to include a bank as well. The Committee recommends that "company" be defined in section 1 of the Act to include any body corporate including a bank so that the word "bank" may be deleted from section 157 and the word "company" where used therein will include banks as well as other bodies corporate.

10.09 The Committee reviewed sections 152 and 155 of the Act which were added to the Act in 1970,[13] and which confer limited power on registered corporations to invest their own funds in the fully paid shares of certain other companies. These companies are described in the regulations under the headings "ancillary business corporation"; "foreign loan corporation"; "foreign trust corporation"; "mutual fund corporation"; "mutual fund sales or management corporation" and "real estate corporation".[14] The regulations define, in considerable detail, the terms and conditions under which a registered company may invest its funds in the shares of any such corporation. The Committee understands that these relatively new investment provisions of the Act have not thus far been extensively used by Ontario corporations. In view of their recent enactment and apparent infrequent use to date, the Committee has con-

cluded that it would be inadvisable for it to make any recommendations with respect to these provisions. Some concern was expressed, however, during the deliberations of the Committee that these provisions might be used as a statutory basis to allow Ontario corporations to proliferate their activities through acquiring subsidiary corporations which carry on a variety of business activities. The Committee therefore favours the restrictive approach taken by the regulations passed pursuant to sections 152 and 155 with respect to investments made thereunder.

10.10 The Committee noted that section 153 (5) of the Act empowers a registered trust company, if properly designated, to lend its own and intermediary funds in guaranteed loans under the Canada Student Loans Act, the Farm Improvement Loans Act (Canada) and the Fisheries Improvement Loans Act (Canada). Unlike section 150 (4) which applies to registered loan corporations, section 153 (5) does not also refer to the Small Businesses Loans Act (Canada). The Committee recommends that section 153 (5) of the Act be amended to include a reference to the Small Businesses Loans Act (Canada).

10.11 **The Committee recommends that:**

(a) the present approach of the Act whereby registered companies may ordinarily invest funds only in investments within the detailed list in section 150 (1) be retained;

(b) section 150 (1) (j) of the Act be amended by deleting therefrom the phrase "to be used on railways or public highways";

(c) a definition of "improved real estate" be inserted in the Act;

(d) sections 151 (b) (ii) and 154 (b) (ii) of the Act be amended by increasing the maximum percentage that may be approved by the Registrar thereunder from 7% to 10%, thereby conferring greater flexibility upon registered corporations to add investments to their basket;

(e) section 157 (1) (a) be amended so that investments in residential mortgages, where the portion of the mortgage loan above 75% of the value of the underlying real estate or leasehold is insured by an insurance company, licensed or registered under the Canadian and British Insurance Companies Act (Canada), the Foreign Insurance Companies Act (Canada), the Insurance Act or similar legislation of any province or territory in Canada, are excepted from the restrictions in section 157 (1) (a);

(f) no change be made in section 157 (1) (b);

(g) section 1 of the Act be amended by adding thereto the following definition:

" 'company' means, unless herein otherwise expressly provided, a body corporate wherever or however incorporated but does not include a corporation to which this Act applies";

and

(h) section 153 (5) of the Act be amended to include a reference to the Small Businesses Loans Act (Canada).

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1. The Trustee Act, R.S.O. 1970, c. 470, sections 26 and 27.
2. The Act, sections 151 (b) (ii) and 154 (b) (ii).
3. The Act, sections 151 (b) (ii) and 154 (b) (ii).
4. Ontario Regulation 435/72 and 436/72.
5. Letter from the Registrar to the Chairman of the Select Committee on Company Law dated February 6, 1975.
6. The Loan and Trust Corporations Act, 1949, S.O. 1949, c. 52, section 131. The Federal Acts do not use the term "improved real estate" but instead prohibit a loan company from lending any of its funds on the security of vacant land not used for agricultural purposes. Loan Companies Act R.S.C. 1970, c. L-12, section 60 (9). Similar restrictions apply to trust companies in respect to loans of trust funds on which interest is payable and loans of trust company funds. See Trust Companies Act R.S.C. 1970, c. T-16, sections 64 (6) and 68 (12).
7. For an example of such a difference of opinion, see The Report of the Royal Commission Appointed to Inquire into the failure of Atlantic Acceptance Corporation Limited, dated September 12, 1969, Vol. 2 at pp. 1039 - 1044. The Report recommends that improved real estate be defined in the Act. See Vol. 3 at pp. 1637-8, 1660 and 1685.
8. The Alberta Act, section 2 (1) 16 provides:
   "improved real estate" means real estate
   (i) upon which there exists a building used or capable of being used for residential, commercial, industrial, educational, religious, charitable or recreational purposes, or
   (ii) upon which such a building is being constructed, or
   (iii) which is provided with the utilities necessary to serve such a building with electric power, water and sewers but only when the land is being mortgaged for the purpose of financing the construction of such a building, or
   (iv) on which actual farming or ranching operations are being conducted.
9. The Land Speculation Tax Act, 1974, S.O. 1974, c. 17, as amended 1974, c. 107; and 1974, c. 121.
10. The Land Speculation Tax Act, 1974, as amended, section 4 (k) (iii) (D).
11. Bank Act, R.S.C. 1970, c. B-1.
12. Association's brief, p. 37-38.
13. Sections 152 and 155 were added to the Act by The Loan and Trust Corporations Amendment Act, 1970 (No. 2), S.O. 1970, c. 129, sections 42 and 44. The new sections were amended in 1973 by The Loan and Trust Corporations Amendment Act, 1973, c. 128, sections 17 and 18 which added to each section a new category of subsidiary described as "any company incorporated to provide financing by mortgage or otherwise on real property in the course of construction".
14. O. Reg. 435/72 and 436/72 published in the Ontario Gazette on September 16, 1972. At the time of writing the report, no regulations have been published respecting investments in the shares of the new category of subsidiary, that is "construction finance companies".

CHAPTER 11

Common Trust Funds And Pooled Trust Funds

11.01 Chapter 9 has explained the Committee's concern about the escalating costs of administering small estates and trusts and the strong desire of the Committee that the services of corporate trustees, including their investment expertise, should be available to a wide section of the Ontario public. Attempts have been made in the past to achieve economies in estate administration through use of "common trust funds", but it appears to the Committee that these attempts have not generally been successful. A "common trust fund" is defined in the Act to mean "a fund maintained by a trust company in which moneys belonging to various estates and trusts in its care are combined for the purpose of facilitating investment".[1] The theory behind such a fund, for which provision was first made in the Act in 1950,[2] is that by combining moneys available in a number of small estates or trusts, investments could be made and administered which would not otherwise be available to them on an individual basis. The rules governing common trust funds are set forth in section 85 of the Act and also, at some length, in regulation 570. It would seem that section 85 and regulation 570 were derived from the common trust fund provisions of the banking law of New York State.[3] The Committee noted that under the Ontario legislation: (a) no fund may be established unless it has trust moneys aggregating at least $200,000; (b) no money of any estate or trust shall be admitted to a fund if as a result the estate or trust would then have an interest in the fund in excess of 10% of the book value of the assets of the fund; (c) a fund must be audited annually and a copy of the audit report filed with the Registrar; (d) a trust company may not charge a management fee to a fund; and (e) a trust company may not publicize the performance record of its fund except as permitted or required by regulation 570.[4] The Committee was advised that very few trust companies are operating common trust funds in Ontario today and that the assets of common trust funds that are being operated represent a small percentage of the total assets under administration by the companies concerned.[5] It appeared to the Committee that the existing restrictions were partly responsible for the failure to use common trust funds extensively and that the relevant restrictions were: the prohibition against charging a management fee to the fund; the limitation on contributions from a single estate or trust; the inability to publicize the fund; the contingency of having to pass accounts in the Surrogate Court; and the limitation of participants to estates and trusts in Ontario. It appeared to the Committee that the problem of the under-utilization of common

trust funds would not be solved simply by changing these and other applicable restrictions, because the trust companies had not shown any great interest in common trust funds as a medium of investment for estates and trusts.[6] The companies indicated considerably more interest in their pooled trust funds and made a submission to the Committee that the Act should be changed to permit a trust company to invest estate and trust moneys in these funds.

11.02 A "pooled trust fund" is defined in section 86 (1) of the Act as,

> "a trust fund maintained or operated by a trust company in which moneys belonging to various participants are combined for the purpose of investment and entitling the participant to receive on demand, or after a specified period after demand, an amount computed by reference to the value of a proportionate interest in the assets of such trust fund, but does not include a trust fund operated where participation is limited to less than fifty persons."

Trust companies began operating these pooled funds, which are similar to mutual funds, in the early 1960's, and by 1973 some eleven companies registered in Ontario were operating pooled funds with total assets throughout Canada of approximately $608 million.[7] Pooled funds have been used as investment vehicles for pension funds and registered retirement savings plans and units in these funds are also sold to the public by some companies. Several companies operate a number of pooled funds, with differing investment objectives, which enables them to offer several investment alternatives to their clients; alternatives which are not available to estates and trusts investing in common trust funds. As mentioned above, the Committee was asked to consider amending the Act so that estate and trust funds could be invested in pooled trust funds which have gained wider acceptance than common trust funds. The Committee understands that the terms of the agreement creating a pooled trust fund normally preclude the trustee from investing assets of the fund in its own guaranteed certificates or receipts. Such a restriction is necessary, in the Committee's view, in order to prevent a trust company from investing estate funds indirectly in its own receipts or certificates — a proposal which was rejected by the Committee in paragraph 9.08 which deals with the direct investment of estate funds in receipts or certificates. The Committee also notes that the trustee normally charges an annual management fee to the pooled trust fund based upon the value of the assets of the fund at various periods throughout the year. If the Act permitted the investment of estate funds in a pooled trust fund, the trustee would receive double remuneration as trustee of the estate unless the value of the units held for the estate was excluded when determining the trustee's remuneration for administering the estate. In the Committee's opinion, the value of the units should be so excluded. The Committee has con-

cluded that the submission received in this connection has merit and the Committee therefore recommends that the Act be amended so that a trust company registered under the Act may invest the moneys held in estates or trusts of which it is trustee or co-trustee in a pooled trust fund maintained or operated by the company in accordance with the Act subject to the proviso that: (1) the terms of the agreement creating the pooled trust fund prohibits the trustee from investing moneys of the fund in the guaranteed investment receipts or certificates of the trustee, and (2) the value of the units held for an estate or trust shall not be included as an asset of the estate or trust when calculating the company's remuneration as executor or trustee of the estate or trust.

11.03 The Committee noted that subsections (4) to (7) of section 86 contain provisions relating to the filing of information folders with the Registrar, such folders to provide brief and plain disclosure of all material facts relating to the pooled trust fund concerned. Subsection (8) of section 86 provides for the making of regulations prescribing, among other things, the form and content of information folders. The Committee understands that no regulations have been made pursuant to section 86 (8) and that the Registrar has not considered it necessary to exercise his discretionary powers under section 86 (4) to require trust companies to file information folders with him. Instead, the practice is being followed of requiring a trust company that offers units in a pooled trust fund to the public to file a prospectus with the Ontario Securities Commission. The Committee was unable during its hearings to inquire into the securities law questions raised by section 86 and therefore makes no recommendations concerning either the present practice that is being followed or the alternative approach suggested by section 86, that is, the filing of information folders with the Registrar.

11.04 The common trust fund provisions of the Act represent an exception to the general rule that trust companies must keep moneys and securities in separate accounts for each individual trust under their administration. The Trust Companies Act (Canada) contains an express provision to that effect.[8] There is no express provision in the Act but the Committee understands that the general practice is for all trust companies registered in Ontario to maintain securities in separate accounts. The Committee heard a submission from the Association urging that provision be made to permit trust companies in Ontario to commingle securities held for different trusts under their administration. Instead of holding separate certificates or other instruments for each trust, a trust company should be permitted to hold one certificate or instrument representing the total holdings of all trusts of which the company is trustee. The submission made it clear that accounting records would be maintained for each trust showing its entitlement to a portion of the securities

represented by the certificate or instrument. It was submitted that commingling would reduce the costs of administering trusts without reducing the amount of information available to the beneficiaries of a trust. The Committee did not have sufficient time at its disposal to examine all aspects of this submission including, for example, the question of whether the existing rights of creditors of a trust company or of an individual trust might be altered by commingling of trust assets. The Committee is of the opinion, however, that trust companies should be permitted to commingle trust assets as long as (a) separate accounting records are maintained for each individual trust; (b) the beneficiaries are entitled to receive the same amount of information that they now receive and with the same promptness; and (c) the rights of creditors are not adversely affected. The Committee understands that a securities depository known as The Canadian Depository for Securities Limited has been incorporated under the Canada Corporations Act, with head office in Toronto, and that one of the objectives of this company is to act as a depository for the securities held by financial institutions including trust companies. In order for trust companies to participate fully in such a depository, it may be necessary or desirable for them to commingle securities held for different trusts. The Committee recommends therefore that any provision added to the Act to permit trust companies to commingle assets of different trusts should also permit them to commingle trust assets within, or under arrangements made with, a securities depository approved by the Registrar.

11.05 **The Committee recommends that:**

(a) the Act should be amended so that a trust company may invest the assets of trusts of which it is trustee in pooled trust funds maintained or operated by such trust company; and

(b) trust companies be permitted to commingle assets held by them either internally or externally through a securities depository approved by the Registrar on condition that:

  (i) separate accounting records are maintained by the trust companies for each individual trust;

  (ii) the beneficiaries of the trusts will be entitled to receive the same amount of information concerning the trust that they now receive and with the same promptness; and

  (iii) the rights of creditors of the trust companies and of the trusts of which they are corporate trustee not be adversely affected.

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1. The Act, section 85 (1).
2. The Loan and Trust Corporations Amendment Act, 1950, S.O. 1950, c. 38, section 2.

3. See McKinney's Consolidated Laws of New York, 1971 Vol. 4 Banking Law, section 100-C, pp. 192 - 215. The Committee was advised during the New York hearings that common trust funds are extensively and, it appears, successfully used by the New York banks. The New York State Bankers Association has also sponsored since 1955 a common trust fund known as "Bank Fiduciary Fund" for use by the smaller banks with trust departments. In 1970 this fund was separated into two funds, an equity fund and a fixed income fund, and these two funds had assets between them of some $50 million in 1974.
4. Ontario Regulation 570, section 2 (1); section 5 (1); section 13; section 15 (1) and section 16.
5. Information Bulletin No. 58 of The Trust Companies Association of Canada dated August 1974 shows that for 1973 only three trust companies operated common trust funds in Ontario. The total value of the funds in operation was approximately $19 million and the total number of participating accounts was 1,856.
6. Association's brief, p. 43.
7. See Information Bulletin No. 58 of The Trust Companies Association of Canada dated August 1974 at pp. 9 and 10. Total assets in equity funds were approximately $166 million and in fixed income funds were approximately $443 million.
8. Trust Companies Act, R.S.C. 1970, c. T-16, section 66 (1) which provides:
   "The moneys and securities given, acquired or held in trust by the company, shall always be kept distinct from those of the company, and in separate accounts, and so marked for each particular trust as always to be distinguished from any other in the registers and other books of account to be kept by the company, so that at no time shall trust moneys form part of or be mixed with the general assets of the company."

CHAPTER 12

By-Laws

12.01 This chapter and the following two chapters on directors and officers and books and records deal with matters relating to the internal affairs of loan and trust companies. The matters discussed primarily concern Ontario incorporated loan and trust corporations although in a few instances, which will be expressly referred to, federal and extra-provincial companies are affected as well. The Committee approached the general subject of the internal affairs of loan and trust corporations by examining in some detail the relevant provisions of the Act and, after having noted and discussed those provisions, the Committee considered the comparisons offered by the BCA. The Committee discovered that in a good many instances the provisions of the two Acts were not the same, and this gave rise to the general question of whether there were any substantive reasons for the differences. In the absence of an adequate reason for a distinction, the Committee favoured adoption of the BCA provision in order to remove, where possible, distinctions between the legal rules that apply to the internal affairs of business corporations incorporated under the BCA and loan and trust corporations incorporated under the Act.

12.02 The sections of the Act relating to by-laws may be roughly divided into those sections that concern the first by-laws of a newly incorporated corporation (sections 3 to 7), and those that concern the powers of the shareholders and directors to enact by-laws (sections 27 to 33). Dealing with the newly incorporated corporation first, the Act provides that the promoters of the new corporation shall hold a meeting prior to filing the application for incorporation "to constitute themselves a provisional corporation . . . under The Loan and Trust Corporations Act and under the proposed by-laws there and then adopted . . .".[1] Three copies of the proposed by-laws must be filed with the application, one copy being duly certified.[2] The Act requires the following matters to be provided for or stated in the by-laws: proposed corporate name and location of head office; the purposes or "objects" of the corporation; the capital of the corporation including particulars of each class of share and, in the case of preference shares, a statement of preferences, rights, conditions, restrictions, limitations or prohibitions attaching thereto; in the case of a loan corporation, a statement to define and regulate the exercise of the borrowing powers conferred by the Act on such a corporation; the holding of shareholders' meetings; the election of directors, their number, powers, duties and term of office, and the number necessary to

constitute a quorum; the security to be taken for the fidelity of persons having custody or control of the funds of the corporation; and amendment of the by-laws by the shareholders in general meeting.[3] The Act further states that if, on receiving an application for incorporation, the Minister finds in the by-laws anything repugnant to the Act or to the law of Ontario, he may direct an amendment of the by-laws, and, upon their being amended as directed and returned certified as having been so amended, the application may be proceeded with.[4] Finally, section 7 of the Act provides in effect that the by-laws accompanying the application, with such amendments as the Minister may require under section 6 of the Act, are the first by-laws of the corporation and take effect on the date of the incorporation.

12.03 The Committee noted that there was a number of differences between the provisions just described and those that apply to a business corporation under the BCA. The Act requires the by-laws to be adopted prior to incorporation, whereas by-laws are not passed until after incorporation under the BCA. The Act requires certain matters to be provided for in the by-laws, whereas the BCA has no such mandatory requirement; certain matters that must be provided for in the by-laws, such as the objects and the capital of the corporation, are dealt with in the articles of a business corporation and not in its by-laws; and there is no all-encompassing requirement that the by-laws of a business corporation need be filed.[5] The Committee was advised that the practice has been for the Registrar to furnish the promoters with a suggested form of first by-laws to be passed at the pre-incorporation meeting. The form prepared by the office of the Registrar is intended, no doubt, both as a guide and as a means of obviating the need for Ministerial amendment under section 6. The Committee noted that the suggested form of by-law contains clauses of a substantive nature dealing with matters, mostly having to do with the directors, that are not covered by sections of the Act. The Committee was of the opinion that sections 4 and 6 of the Act, when viewed in the context of the present practice of a departmental form of suggested by-laws containing clauses that do not flow from individual sections of the Act, may introduce an element of discretion to impose restrictions upon the internal affairs of Ontario corporations. The Committee questioned the need for such a discretion and was concerned that matters such as those relating to disclosure by directors of interests in contracts and the indemnification and removal of directors, are not provided for in the Act, as they are in the BCA, but are governed instead by the by-laws. The Committee is of the opinion that loan and trust corporations should have the same freedom as business corporations to adopt by-laws not contrary to the Act or to their letters patent, regulating their internal affairs, and that any controls deemed necessary to regulate

the exercise by them of their borrowing powers, the conduct and removal of their directors, and the security to be furnished by persons having custody or control of a corporation's funds should be imposed by express provisions of the Act in the areas where these matters are dealt with. The Committee has already recommended in Chapter 3 that the notion of a provisional corporation and the requirement for a pre-incorporation meeting be deleted from the Act, and some change is required therefore in the procedure to be followed in adopting by-laws. For these reasons, the Committee recommends that there no longer be any requirement in the Act to pass by-laws prior to incorporation or to submit draft by-laws with the petition for incorporation. By-laws should be passed by the directors and shareholders in the normal way after incorporation, and in due course a certified copy should be delivered to the Registrar under section 30 of the Act. It follows from this recommendation, that sections 4, 6 and 7 of the Act should be repealed. Matters relating to directors that, in the Committee's view, should be dealt with in the Act and not just in the by-laws will be discussed in Chapter 13. Since the sections to be recommended will be different from the corresponding sections in the departmental suggested form and may also be different from provisions in the by-laws of existing Ontario corporations, a transitional section based on section 272 of the BCA should also be added to the Act.

12.04 The other main part of the Act relating to by-laws is to be found in sections 27 to 33. Section 27 provides that a meeting of the shareholders, called with due notice thereof, may make such lawful and proper by-laws for the government of the corporation, not repugnant to the Act or any other law in force in Ontario, as the majority of the shareholders present in person or by proxy consider proper. This section, which confers enacting power on the shareholders, departs from the general rule applicable to most business corporations which is that the directors ordinarily enact the by-laws and the shareholders either confirm, reject or amend what the directors have done.[6] It appears that the unusual provision of the Act originated in the building society legislation of Ontario from which the Act is derived. The Building Society Act of 1859 provided that "The several members of the Society may from time to time assemble together, and make such proper rules for the government of the same as the majority of members so assembled deem meet . . .".[7] The language bears a close similarity to that of section 27. The wide power conferred by section 27 appeared to the Committee, however, to be illusory. In practice the shareholders delegate power to the directors to make, amend and repeal by-laws of the corporation under section 31 of the Act, and the directors, acting under this power, pass all by-laws of the corporation subsequent to its first by-laws, the role of the shareholders being limited to confirming, rejecting or amending what the

directors have done. Thus, by-laws are passed in the same way as they are for business corporations. Quite apart from the matter of the enacting power which has just been described, the Committee considers that the intent and wording of sections 31, 32 and 33 of the Act are not entirely clear. For example, is section 33, which empowers the directors to make by-laws regulating the five enumerated matters in section 33, including the very broad enumerated matter in subsection (e), intended to limit the authority of the shareholders to delegate powers to the directors under section 31 (1)? Again, what is the distinction between the power of the "corporation" under section 31 (3) to repeal, amend, vary or otherwise deal with any by-law passed by the directors and the power of the shareholders under section 32 at a general meeting to alter or amend "such by-laws" and to confirm them as so altered and amended? The Committee considers that it would be preferable to amend the Act so as to conform more closely to the present day realities of how by-laws are passed and to remove any questions of interpretation that may arise under the present wording of sections 31 to 33. Accordingly, the Committee recommends that sections 27, 31, 32 and 33 of the Act be repealed and that a section similar to section 21 of the BCA be substituted in their place. The directors of Ontario corporations will then have full power to enact by-laws which the shareholders may confirm, reject or amend.

12.05 The Act provides that every corporation shall deliver to the Registrar within one month after the passing thereof, a certified copy of its by-laws and of every repeal, or addition thereto or amendment or consolidation thereof.[8] This provision applies to federal and extra-provincial companies in addition to Ontario corporations.[9] The Act also provides that the by-laws of Ontario corporations shall be reduced to writing and recorded in a book to be kept by the corporation known as the "by-law book".[10] Under the Act, the by-law book shall, without payment of any fee or charge, be open during business hours for inspection by any shareholder, depositor, debenture holder or holder of a guaranteed investment certificate, by himself or his agent, and any such person may make extracts therefrom.[11] The Committee considered, in relation to these provisions, the constructive notice doctrine whereby third parties are deemed to have notice of the contents of documents of a corporation filed in a public office. The Committee was advised that copies of by-laws of registered corporations filed with the Registrar are not open to public inspection and consequently, it appeared to the Committee that filing with the Registrar would not constitute filing in a "public office". However, the Committee considers that *any* person should be permitted to inspect by-laws on file with the Registrar and accordingly, the Committee recommends that section 30 of the Act be amended to confer such right of inspection. Since this amendment would give rise to the

operation of the constructive notice doctrine, the Committee further recommends that a new section be added to the Act based on section 17 of the Canada Business Corporations Act and to read as follows:

> "No person is affected by or is deemed to have notice or knowledge of the contents of a by-law of a corporation by reason only that the by-law has been filed with the Registrar or is available for inspection at an office of the corporation."[12]

12.06 The Committee is aware that the Act does not use the defined terms "special by-law" and "special resolution" contained in the BCA.[13] A special by-law is defined in the BCA as follows:

> " 'special by-law' means a by-law that is not effective until it is,
>
> i. passed by the directors of a corporation, and
>
> ii. confirmed, with or without variation, by at least two-thirds of the votes cast at a general meeting of the shareholders of the corporation duly called for that purpose, or such greater proportion of the votes cast as the articles provide, or, in lieu of such confirmation, by the consent in writing of all the shareholders entitled to vote at such meeting or their attorney authorized in writing;"

The definition of special resolution is to the same effect. The term "special by-law" is used in the BCA in relation to the authorization of matters of a continuing nature, for example, the power to borrow money; the term "special resolution" is used in relation to the authorization of a non-continuing matter such as the approval of an application for articles of amendment.[14] The Committee recommends that definitions of both terms be added to the Act and that under the new Act, the following matters should require authorization by a special by-law: change of head office; change in the number of directors; formation of an executive committee; creation of the office of chairman of the board; and authority to exercise the borrowing powers and intermediary powers conferred by the Act. The Act should provide that an Ontario corporation wishing to change its name should be required to apply for supplementary letters patent changing its name and that the application should be authorized by special resolution. Grant of the supplementary letters patent should be at the discretion of the Minister without, in the Committee's opinion, any requirement for an order in council. Changes in authorized capital, which will be discussed more fully in Chapter 15, should be handled in the same manner as a change of name.

12.07 The Act was amended in 1973 to provide that an Ontario loan corporation may apply by petition to the Lieutenant Governor in Council for an order designating it as a "mortgage investment company".[15] Under

the Act, "a loan corporation that is designated as a mortgage investment company shall not commence business as a mortgage investment company until its by-laws have been amended to conform to the terms and conditions prescribed, the provisions of sections 17b to 17f, and the regulations and such by-laws have been filed with and approved by the Registrar."[16] It appears to the Committee that this provision is in conflict with its recommendations in this Chapter. The Committee did not have sufficient time to examine in detail sections 17a to 17h of the Act which relate to mortgage investment companies, and consequently does not consider that it should recommend any changes to those sections. The Committee would simply make the observation, however, that if consistency is to be maintained between its recommendations in this Chapter and section 17a (4) of the Act, which is quoted in this paragraph, any restrictions respecting the affairs of mortgage investment companies should be stated in the Act or regulations and not in their by-laws.

12.08 **The Committee recommends that:**

(a) Ontario corporations should be permitted to pass general by-laws in the normal way after incorporation and be able to include in their by-laws any provision that is not contrary to the Act, the regulations, or their letters patent;

(b) a certified copy of the first by-laws of an Ontario corporation should be filed with the Registrar within one month after their passing;

(c) sections 4, 6 and 7 of the Act should be repealed;

(d) a transitional section based on section 272 of the BCA should be added to the Act so that existing Ontario corporations whose by-laws contain provisions that conflict with the new Act will be given time to amend their by-laws as may be required;

(e) the directors of an Ontario corporation should be given full power to enact by-laws for the corporation, and the role of the shareholders should be confined to confirming, rejecting or amending any by-law enacted by the directors;

(f) sections 27, 31, 32 and 33 of the Act should be repealed;

(g) section 30 of the Act should be amended to provide that any person may inspect in the office of the Registrar the certified by-laws of a registered corporation on file in his office;

(h) a new section should be added to the Act to make it clear that the right to inspect by-laws of a registered corporation in the office of the Registrar or the head office of the corporation does not give rise to the application of the constructive notice doctrine;

(i) the defined terms "special by-law" and "special resolution" should be added to the Act and the following matters should require prior authorization by special by-law:
   1. change of head office;
   2. change in the number of directors;
   3. formation of an executive committee;
   4. creation of the office of chairman of the board; and
   5. exercise of the borrowing powers and intermediary powers conferred by the Act;

(j) a change of name should be authorized by special resolution and effected by the grant of supplementary letters patent at the discretion of the Minister; and

(k) a change in authorized capital should be authorized by special resolution and effected by the grant of supplementary letters patent at the discretion of the Lieutenant Governor in Council.

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1. The Act, section 3 (6).
2. The Act, section 4 (1).
3. The Act, section 4 (2).
4. The Act, section 6.
5. Under sections 124 (2) and 14 (4) of the BCA, a by-law changing the number of directors of a business corporation or changing the locality of its head office must be filed with the Minister.
6. See section 21 of the BCA. Note that section 101 of the BCA introduces a new procedure whereby the holders of at least ten per cent of the voting rights attached to equity shares of a corporation can set proceedings in motion which might result in a by-law being passed by the shareholders.
7. The Building Societies Act, Statutes of the Province of Canada, 1859, 22 Vic., c. 53, section 2.
8. The Act, section 30.
9. The Act, section 2 (3).
10. The Act, sections 28 and 29 (1).
11. The Act, section 29 (2).
12. Canada Business Corporations Act, S.C. 1974-75, c. 33.
13. The BCA, section 1 (1) 26 and 27.
14. See Lavine, The Business Corporations Act — an Analysis, (Carswell: Toronto, 1971 at pp. 19 and 20).
15. The Act, section 17a (1), which was added to the Act by The Loan and Trust Corporations Amendment Act, 1973, S.O. 1973, c. 128, section 5.
16. The Act, section 17a (4).

CHAPTER 13

Directors and Officers

13.01 The nature of the business conducted by loan and trust companies, in particular their deposit-taking, intermediary and trust functions, demands managerial competence in their directors and officers of the highest order. To some degree, the Act acknowledges the importance of managerial expertise when, in the context of an application to incorporate a new company, it refers to the fitness of the applicants — or first directors — to discharge the duties of a trust or loan company.[1] Again, in the context of an application to register an extra-provincial trust company, the Act requires the Registrar to be satisfied that the fitness of the applicant to discharge the duties of a trust company is such as to command the confidence of the public.[2] Fitness of a company is presumably determined by reference to the competence of its management.

Although these matters are not expressed in the Act as continuing requirements (which is recommended, however, in paragraph 4.08), there is little doubt that they are so regarded by the Registrar, who must supervise the companies on a continuing basis, and by the companies themselves who are well aware of the interrelationship between managerial competence and maintenance of public confidence which is so essential to the business being conducted. The Act requires each director to hold, in his own right, more than just a nominal share interest in the corporation; generally speaking an investment of at least $2,500 is required by each director.[3] Each corporation must report annually to the Registrar the names, addresses, shareholdings and citizenship of its directors and officers.

The Act imposes a number of specific duties and liabilities upon directors, including a duty not to declare or pay dividends or bonuses that render the corporation insolvent;[4] liability for certain unpaid wages of the servants of a corporation;[5] liability where shares of the corporation are transferred contrary to the provisions of the Act;[6] liability for any deficiency when unauthorized investments are disposed of as required by the Registrar;[7] and liability for wilfully false or deceptive statements in any account, statement, return, report or other document respecting the affairs of the corporation.[8] These sections serve to illustrate the importance which the Act already attaches to the role of the director and, to a lesser extent, to the officer. It appeared to the Committee, however, after a review of the provisions of the Act concerning directors and officers and a comparison with the relevant sections of the BCA, that the Act is not as up-to-date as it should be and that certain amendments and additions are required. These will now be examined.

13.02 The Act does not expressly provide, as the BCA does,[9] that the board of directors shall manage or supervise the management of the affairs and business of the corporation. It is usual, however, for the first by-laws of an Ontario corporation to contain a clause entrusting to the board of directors the responsibility for the management of the corporation's affairs.[10] The Committee considers that this clause should also be stated affirmatively in a section of the Act and recommends therefore that a new section be added to the Act as follows:

> "The board of directors shall manage or supervise the management of the affairs and business of the corporation."

The Act contains two sections, 38 and 41, concerning the matter of the powers of the directors. There appears to be no equivalent to these sections in the BCA. Section 38 provides that:

> "The directors may lawfully exercise all the powers of the corporation except as to such matters as are directed by law or by the by-laws of the corporation to be transacted at a general meeting and have not been delegated to the directors by a general meeting as provided by section 31."

It appeared to the Committee that very few matters were directed by the Act or the by-laws to be transacted at a general meeting of shareholders[11] and that in fact the powers conferred on the directors by section 38 were very broad. Such broad powers are required by the directors in order to discharge their responsibilities of management under the provision recommended for inclusion in the Act by this paragraph 13.02. The Committee concluded therefore that section 38 should be retained subject to the deletion of the concluding phrase "and have not been delegated to the directors by a general meeting as provided by section 31" which is no longer required in view of the Committee's recommendation in Chapter 12 that section 31 be repealed. Section 41 of the Act provides:

> "Subject to this Act and to the Act or instrument constituting the corporation and to the by-laws of the corporation, the directors may,
>
> (a) use or cause to be used and affixed the seal of the corporation, and may affix or cause it to be affixed to any document or paper that in their judgment requires it;
>
> (b) make and enforce calls upon the shares of the respective shareholders;
>
> (c) declare the forfeiture of all shares on which calls are not paid;
>
> (d) make any payments and advances of money they consider expedient that are authorized to be made by or on behalf of the corporation, and enter into all contracts for the execution

of the purposes of the corporation, and for all other matters necessary to the transaction of its affairs;

(e) generally deal with, sell, exchange, lease and dispose of the lands, property and effects of the corporation in such manner as they consider expedient and conducive to the benefit of the corporation;

(f) do and authorize, assent to or adopt all acts required for the due exercise of any further powers and authorities conferred by the Legislature."

The Committee considers that section 47 of the Act confers upon the directors whatever powers they may require in respect to items (b) and (c) of section 41. The Committee also considers that the remaining items of section 41 could be more appropriately dealt with in the by-laws of the corporation and do not require specific mention in the Act. Accordingly, the Committee recommends that section 41 of the Act be repealed.

13.03 Having concluded that the duty to manage or to supervise the management of the business and affairs of an Ontario corporation rests with its directors, the Committee next had to consider whether the Act should contain a statement of the standard of care, diligence and skill owed by a director to the corporation in the discharge of his office. This question was considered at length with reference to the directors of a business corporation by the Select Committee in its interim report of 1967. Its recommendation that a standard of care for directors should be enacted was adopted and is now found, substantially worded as recommended by the Committee in 1967, in section 144 of the BCA which reads as follows:

"Every director and officer of a corporation shall exercise the powers and discharge the duties of his office honestly, in good faith and in the best interests of the corporation, and in connection therewith shall exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances."

The section applies to both directors and officers of a business corporation. There have been no reported case decisions on section 144 to date, so far as the Committee is aware. Several older case decisions of the Canadian courts where the liability of the directors of a trust company or loan company was at issue were referred to the Committee but these cases were not particularly helpful to the Committee in describing the duty owed by such directors to their corporations.[12] The best statement, and one which still appears to apply to the directors of Ontario loan and trust corporations, is to be found in the judgment of Romer J. in *In re*

City Equitable Fire Insurance Company, Limited,[13] an English Court of Appeal decision involving a large reinsurance company which was in liquidation. While on the facts of the case the directors were found to have been in breach of their duty of care and skill to the company, they escaped liability because of a clause in the company's articles which indemnified them against any loss suffered by the company except a loss incurred by their own wilful default. Romer J. summarized the common law duty owed by a director as follows:

> "(1) A director need not exhibit in the performance of his duties a greater degree of skill than may reasonably be expected from a person of his knowledge and experience.
>
> (2) A director is not bound to give continuous attention to the affairs of his company. His duties are of an intermittent nature to be performed at periodical board meetings, and at meetings of any committee of the board upon which he happens to be placed. He is not, however, bound to attend all such meetings, though he ought to attend whenever, in the circumstances, he is reasonably able to do so.
>
> (3) In respect of all duties that, having regard to the exigencies of business, and the articles of association, may properly be left to some other official, a director is, in the absence of grounds for suspicion, justified in trusting that official to perform such duties honestly."[14]

In the Committee's opinion, the standard of care and skill to be observed by a director or an officer of an Ontario corporation should be a higher duty than that described by the three propositions just mentioned. The Committee recommends that a statutory standard of care, diligence and skill should be set forth in the Act and to that end, and with a view to raising the standard, the Committee recommends that the following section be added to the Act:

> "Every director and officer of a provincial corporation shall exercise the powers and discharge the duties of his office honestly, in good faith and in the best interests of the corporation, and in connection therewith shall exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances."

Except for the minor change of "corporation" to "provincial corporation", the proposed section is identical to section 144 of the BCA. This is not to say that the Committee considers the standard of conduct to be observed by a director or officer of a loan or trust company to be the same as the standard for a director or officer of a business corporation. The directors and officers of a loan or trust company have in their care,

and under their management, funds drawn from a wide section of the public and, in the Committee's view, this fact plus the other facets of businesses of these companies imposes upon their directors and officers a high standard of conduct in performing their functions.[15] The Committee is confident that the statutory standard recommended for inclusion in the Act in this paragraph 13.03 will be understood and, where necessary, applied by the courts, in recognition of the high standard owed by directors and officers of these companies. Hughes J. in the Report of the Royal Commission appointed to inquire into the failure of Atlantic Acceptance Corporation Limited[16] (hereinafter referred to as the "Atlantic Report"), expressed concern that section 144 (as then proposed) might expose a director to suit where the director had committed an error in judgment but there had been no bad faith, fraud or negligence on the director's part. He recommended that when the Act was revised, a provision should be added to the effect that:

> "No action should be brought against any director or officer of a trust company to enforce any right, duty or obligation owed to his company only on the ground that an action taken or decision made by him was not in the best interests of the company, unless it is alleged that such action was taken or decision made fraudulently, negligently or in bad faith."

The Committee considered this recommendation and, based upon the Committee's understanding of section 144, concluded that it did not need to be implemented. In the Committee's opinion, the word "and" which follows "corporation", in the fourth line of section 144 is intended to be read conjunctively with the result that the concluding phrase "and in connection therewith shall exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances" modifies the previous part of the section including the director's duty to act "in the best interests of the corporation."

13.04 In dealing with the by-laws in Chapter 12, it was mentioned that the Act contains no section providing for the indemnification of directors and officers. An indemnity clause is, however, normally contained in the standard first by-laws[17] and it would appear to follow the language of section 81 of The Corporations Act.[18] The right to indemnity enjoyed by a director or officer of a business corporation under the BCA is narrower than that afforded under The Corporations Act and the Committee considers that the narrower right should be applied to the directors and officers of loan and trust corporations. The Committee therefore recommends that the following section be added to the Act:

"(1) Subject to subsection 2, the by-laws of a provincial corporation may provide that every director and officer of the corporation and his heirs, executors, administrators and other legal personal representatives may from time to time be indemnified and saved harmless by the corporation from and against,

(a) any liability and all costs, charges and expenses that he sustains or incurs in respect of any action, suit or proceeding that is proposed or commenced against him for or in respect of anything done or permitted by him in respect of the execution of the duties of his office; and

(b) all other costs, charges and expenses that he sustains or incurs in respect of the affairs of the corporation.

(2) No director or officer of a provincial corporation shall be indemnified by the corporation in respect of any liability, costs, charges or expenses that he sustains or incurs in or about any action, suit or other proceeding as a result of which he is adjudged to be in breach of any duty or responsibility imposed upon him under this Act or under any other statute unless, in an action brought against him in his capacity as director or officer, he has achieved complete or substantial success as a defendant.

(3) A provincial corporation may purchase and maintain insurance for the benefit of a director or officer thereof, except insurance against a liability, cost, charge or expense of the director or officer incurred as a result of a contravention of [duty of care] section . . . "

The Committee is aware that the foregoing recommendation does not agree with one of the recommendations of Hughes J. in the Atlantic Report.[19] Hughes J. criticized the foregoing section, as it appeared in Bill 125, introduced in the Legislature in 1968 and ultimately enacted, in amended form, as the BCA, and he concluded by recommending that the indemnification by a trust company of a director or officer against whom such a derivative action has been brought by a shareholder should be a question for its shareholders other than the defendant director or officer. It appeared to the Committee that this recommendation arose, to a great extent, from the learned Judge's concern over the terms of the proposed new section authorizing shareholders' derivative suits. This section, which is now section 99 of the BCA, will be discussed further in paragraph 16.02. Insofar as the indemnification section itself is concerned, the Committee does not consider that a distinction between a director or officer's right to indemnity should be made between the BCA and the Act and accordingly, with deference, does not concur with the recommendation of Hughes J.

13.05 The Act contains no section imposing upon the director of an Ontario corporation a duty to declare his interest at a meeting of the directors of the corporation in any contract or transaction to which the corporation is or is to be a party. The suggested form of first by-laws prepared by the office of the Registrar contains such a clause, but on review of the clause by the Committee and on comparison with the disclosure requirements of section 134 of the BCA, the clause appeared to have a number of deficiencies. The Committee considers that the requirement to disclose any interest in a contract or transaction should be stated in the Act and therefore recommends that the Act be amended by adding thereto a section based on section 134 of the BCA.

13.06 The Act imposes a duty on the directors of an Ontario corporation not to declare or pay any dividend or bonus when the corporation is insolvent, or that renders the corporation insolvent or diminishes its capital.[20] The section goes on to describe what action a director who disagrees with the payment of the dividend or bonus should take in order to exonerate himself. Upon comparison of this provision with the comparable sections of the BCA,[21] it appeared to have the following weaknesses: (i) it does not prohibit the corporation from paying the dividend or bonus; (ii) it does not impose personal liability upon the directors for any such dividend or bonus so paid, nor does it provide a procedure whereby any person receiving the dividend or bonus may be made jointly and severally liable with the directors for repayment of the amount received by such person; and (iii) the procedures whereby a director may dissociate himself from the payment are not as tightly drawn as those of the BCA. The Committee recommends that the Act be amended by adopting the approach followed in sections 136 and 137 of the BCA and by amending section 45 so that the corporation itself is also prohibited from paying the dividend or bonus. The Committee noted that the Act does not impose a liability upon directors where preference shares are redeemed for cancellation in circumstances which render the corporation insolvent. The Committee recommends that a new section based on section 135 of the BCA be added to the Act imposing personal liability upon directors in the circumstances just described. The new section should also impose liability where the directors authorize a corporation to purchase its own common shares and the purchase renders the corporation insolvent. Reference should be made to paragraph 15.03 where the Committee recommends that an Ontario corporation be empowered to purchase its own common shares out of surplus.

13.07 Section 46 of the Act imposes liability, subject to the terms of the section, upon the directors of all registered corporations for all debts, not exceeding one year's wages, for services performed to the corporation

the BCA, section 139, imposes a similar liability upon the directors of a by its "labourers, servants and apprentices". The comparable section of business corporation "to the employees of the corporation to whom The Master and Servant Act applies" but in this case the liability is limited to an amount not exceeding six months' wages. A comparison between the wording of section 46 and section 139 indicated that a number of drafting improvements had been made to section 139 which the Committee considers should be made to section 46 of the Act. Accordingly, the Committee recommends that section 46 be revised to follow the language of section 139 of the BCA, except that the maximum liability under the revised section should remain an amount not exceeding one year's wages and the time period within which to sue the corporation for the debt under subsection (2) of the revised section should be one year instead of six months.

13.08 The Act distinguishes between the "provisional directors", "first directors" and "directors" of an Ontario corporation. Section 15 of the Act provides that where incorporation is granted, the provisional directors named in the declaration of the applicants are the first directors of the corporation, and shall continue in office until their successors are duly elected. The Committee recommends that all references to provisional directors be deleted from the Act and that section 15 be repealed and a new section based on section 123 of the BCA be substituted in its place as follows:

"(1) Each of the persons named as first directors in the letters patent of a provincial corporation is a director of the corporation until replaced by a person duly elected or appointed in his stead.

(2) The first directors of a provincial corporation have all the powers and duties and are subject to all the liabilities of directors."

13.09 The Committee reviewed the provisions of the Act relating to qualification of directors, election of directors, the filling of vacancies on the board, the number of directors and term of election, remuneration of directors and delegation of directors' powers to an executive committee. These provisions are to be found in sections 34, 35, 36, 37 and 40 of the Act. The Committee concluded that amendments should be made to these sections to bring them into line with the comparable provisions of the BCA. No purpose would be served by describing in this report the detail of the necessary amendments since this, in the Committee's view, should be left to the draftsman of the new Act. The Committee considers, however, that it should state some general principles in order to assist the draftsman. The provisions of section 34 of the Act respecting the minimum number of directors and the term of their election

to office do not correspond with the comparable provisions of the BCA. The Committee recommends that the requirements for a minimum number of five directors be retained for Ontario corporations and that there be no change made with respect to their term of office as now provided in section 34. The Committee noted that subsections (2) and (3) of section 35 of the Act contain provisions with respect to the qualification of directors that are not found in the BCA. The Committee recommends that these two subsections be retained in the Act without amendment. Subject to the foregoing and to the exceptions noted below, the Committee recommends that the principles of the BCA relating to qualification of directors, consent to election as director, change in number of directors, filling of vacancies on the board, quorum of directors, place of meetings of the board and of the executive committee, transaction of business at meetings of the board and of the executive committee, removal of directors, election of directors and the remuneration of directors be adopted in the new Act. The Committee did not consider it desirable that the directors of an Ontario corporation should be permitted to act by means of an unanimously signed resolution or by-law or that meetings of the board or the executive committee should be held by means of conference telephone or other communications equipment. Accordingly, the Committee recommends that section 23 (1) and section 130 (3) of the BCA not be followed in the new Act.

13.10 Section 42 of the Act provides as follows:

> "(1) Where the directors entertain reasonable doubts as to the legality of any claim to or upon any share, bond, debenture or obligation of the corporation, or to or upon any dividend, coupon or the proceeds thereof, they may apply to the Supreme Court, stating such doubt, for an order or judgment adjudicating upon such claim, and awarding such share, bond, debenture, obligation, dividend, coupon or proceeds to the person legally entitled to the same, and the court may restrain any action or proceeding against the corporation, or the directors or officers thereof, for the same subject-matter, pending the determination of the application.
>
> (2) If the order or judgment of the court is obeyed, the corporation and the directors and officers are fully protected and indemnified against all actions, claims and demands in respect of the matters in question in such application and the proceedings thereupon."

The Committee reviewed this section and considered whether any changes were required. The Committee's attention was drawn to the fact that it was recommended in the Atlantic Report that the section be changed to provide that the application should in the first place be made to the Registrar with a right of appeal by all parties to the Supreme Court.[22]

The Committee is of the opinion that because the property rights of third parties are involved, the application should be made to the court in the first instance and accordingly, recommends that no change be made to section 42.

13.11 The Committee has recommended in paragraphs 13.03 and 13.04 that new sections be added to the Act providing for a statutory standard of care for "officers" of an Ontario corporation and for their indemnification by the corporation. For the purposes of these sections, the Committee recommends that the following definition be added to section 1 of the Act:

> " 'officer' means the chairman or any vice-chairman of the board of directors, the president, any vice-president, the secretary, any assistant secretary, the treasurer, any assistant treasurer, the general manager, or any other person designated an officer by by-law or by resolution of the directors or any other individual who performs functions for the provincial corporation similar to those normally performed by an individual occupying any such office."

This definition should apply generally throughout the Act, except where a different definition may be expressly adopted.

13.12 The Committee recommends that section 39 (1) of the Act be amended so that vice-presidents are not required to be directors. The Committee also recommends that section 142 of the BCA which provides that a corporation may by special by-law provide for the election or appointment of a chairman of the board be added to the Act.

13.13 The Committee considered section 43 of the Act which provides that:

> "The secretary or treasurer or secretary-treasurer or other officer of the corporation may be styled "Manager", and when the officer is also a director, he may be styled "Managing Director"."

The Committee believes this section, which appears to have originated with building societies, to serve no useful purpose today and recommends that it be repealed.

13.14 The Act was amended in 1974 by the addition of a new section 40a which provides as follows:

> "In addition to the general powers of delegation authorized by section 40, the shareholders of a corporation may, at a general meeting called for the purpose, by resolution of two-thirds of the shareholders present in person or by proxy, authorize the directors to delegate, with or without the power of subdelegation, to the president of the corporation the exercise of any or all powers or

authorities whether discretionary or otherwise, that may arise through the performance of the corporation of its responsibilities under any will, trust, deed, contract or instrument and the exercise of any such power by the president shall in all instances constitute a performance by the corporation of its responsibilities under any will, trust, deed, contract or instrument."

The Committee understands that one of the purposes of the new section is to permit delegation of a discretionary power conferred on a trust company which, under the law as it existed in Ontario before the amendment, had to be exercised by the full board of directors.[23] The Committee was advised that boards of directors, particularly of large trust companies with extensive estates business, were being unnecessarily burdened with a great number of policy decisions of a relatively minor nature and which should, in the Committee's view, be left to a senior officer of the company such as the president. While the Committee welcomes the addition of section 40a to the Act, the Committee recommends that it be amended so that the delegation is effected by special by-law instead of by resolution of the shareholders, which by-law should be required to set forth the terms of the delegation and should require the president to make a report to the board annually summarizing the actions taken pursuant to the by-law during the preceding year.

13.15 **The Committee recommends that:**

(a) the Act be amended to provide expressly that the board of directors shall manage or supervise the management of the affairs and business of an Ontario corporation;

(b) section 38 be amended by deleting therefrom the phrase "and have not been delegated to the directors by a general meeting as provided by section 31";

(c) section 41 of the Act be repealed;

(d) a statutory duty of care for the directors and officers of Ontario corporations be contained in the Act;

(e) a section providing for the indemnification of directors and officers of Ontario corporations, based upon section 147 of the BCA, be added to the Act;

(f) a section providing that the directors must declare any interest in a contract or transaction involving an Ontario corporation or a subsidiary of the corporation, based upon section 134 of the BCA, be added to the Act;

(g) sections 45 and 46 of the Act, respecting payment of dividends or bonuses that render an Ontario corporation insolvent and imposing

liability upon the directors for the unpaid debts owed by the corporation to its servants, be amended to conform more closely to the comparable sections of the BCA;

(h) a new section be added to the Act imposing personal liability upon the directors who authorize any redemption or purchase for cancellation of preference shares or any purchase by an Ontario corporation of its common shares that in either circumstance renders the corporation insolvent;

(i) all references to "provisional directors" be deleted from the Act and a section based on section 123 of the BCA be added to the Act;

(j) the provisions of the Act respecting the qualification of directors, their election, term of election, number, remuneration and removal, the executive committee, the holding of meetings of directors and of the executive committee should, except as noted in paragraph 13.09, be amended to follow the principles with respect to those matters in the BCA;

(k) no change be made in section 42 of the Act;

(l) section 1 of the Act be amended by adding thereto a definition of the term "officer" to apply throughout the Act except where otherwise expressly so provided;

(m) section 39(1) of the Act be amended so that a vice-president need not be a director and a new section be added to the Act providing for creation of the office of chairman of the board;

(n) section 43 of the Act be repealed; and

(o) section 40a be amended to provide for the passing of a special by-law authorizing a delegation of powers, with or without the power of subdelegation, to the president, and that such special by-law should specify the terms of any such delegation and require the president to report to the board annually, summarizing the exercise of such powers pursuant to the delegation during the preceding year.

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1. The Act, section 16 (2).
2. The Act, section 137 (4).
3. The Act, section 35 (2).
4. The Act, section 45.
5. The Act, section 46.
6. The Act, sections 55 (4) and 60 (2).
7. The Act, section 165.
8. The Act, section 176.
9. The BCA, section 132 (1).

10. Paragraph 24 of the general by-law for a trust company in the form suggested by the Registrar provides, in part, that "the affairs of the Company shall be managed by its board of directors".
11. See, for example, section 19 (1) of the Act which describes the business to be transacted at an annual meeting of shareholders. See also those sections of the Act requiring confirmation by the shareholders of a by-law before certain activities may be engaged in, for example, receipt of deposits or moneys for guaranteed investment which require an authorizing by-law under section 89a.
12. See Traders Trust and Kory (1916) 26 D.L.R. 41; Re Dominion Trust Company (1917) 32 D.L.R. 63; and Northern Trust Co. v. Butchart (1917) 35 D.L.R. 169.
13. (1925) Ch. D. 407.
14. (1925) Ch. D. 428-9.
15. See remarks of Romer J. (1925) Ch. D. at p. 426 where he states that the position of a director of a small retail business is very different from that of a director of (a larger company such as) a railway company.
16. Atlantic Report, Vol. 3 at pp. 1510-1513.
17. Clause 39 entitled "Indemnity of Directors and Officers".
18. The Corporations Act, R.S.O. 1970, c. 89.
19. Atlantic Report, Vol. 3 at p. 1651.
20. The Act, section 45.
21. The BCA, sections 153 (3), 136 and 137.
22. Atlantic Report, Vol. 3, pp. 1650-51.
23. See Re Wilson (1937) O.R. 769 where the Ontario Court of Appeal held that a discretionary power to postpone sale of property forming part of an estate could not be delegated by the board of directors to the general manager of the trust company concerned. The attempted exercise of the discretionary power by the general manager was therefore ineffective.

CHAPTER 14

Books and Records

14.01 The Act contains a series of sections devoted to the matter of the books and records that must be maintained by registered corporations. Section 66 (1) describes the books that are to be kept and section 66 (5) provides that these books may be inspected by any shareholder, depositor or holder of an intermediary obligation of the corporation. Section 66a, which was adopted in 1973,[1] empowers any person upon filing an affidavit with the corporation to obtain a list of its shareholders. Sections 67 and 68 contain what appear to be unusual provisions as to the maintenance of registers of securities held by the corporation. Sections 69 and 70 provide that the books are the property of the corporation and provide certain remedies for the recovery of the books and other property of a corporation which are retained by a person against its wishes. Finally, section 71 provides that the books are prima facie evidence of the facts thereby stated. The Committee noted that these seven sections are limited in their application to registered corporations having their head offices in Ontario.[2] For practical purposes, this would seem to cover all Ontario corporations plus those federally incorporated companies that have their head offices in Ontario. The Committee examined the sections of the Federal Acts relating to the obligation of federal companies to keep books and found that the language used in the Federal Acts closely resembles that in section 66 (1) of the Act.[3] It was noted that the Federal Acts go beyond the Act in imposing an obligation to maintain books of account[4] and in requiring loan companies to maintain registers in respect of their debentureholders.[5] A brief examination of the sections of the BCA relating to records[6] revealed quite substantial differences with the provisions of the Act summarized above. To mention but a few examples, a business corporation is permitted to maintain records by means of a mechanical, electronic or other device; a business corporation is required to maintain registers of all its security holders, not just its shareholders, and more detailed information must be entered and maintained in such registers; a business corporation is required to maintain proper accounting records and registers of the transfers of all securities issued in registered form. Express provision is also made in the BCA for branch registers. The Committee considers that some updating and broadening of the requirements of the Act with respect to books and records is necessary. Its recommendations in this connection are set forth in the following paragraphs.

14.02 The Committee has concluded that the general principles to be

found in sections 156 to 166 of the BCA with respect to the maintenance of records; examination or inspection of records; taking extracts therefrom; making lists of security holders or registered warrant holders; obtaining a basic list and supplementary lists of security holders or registered warrant holders; and applications to the court for the rectification of records, should be applied to Ontario corporations. It follows from this recommendation that sections 66, 66a, 69, 70 and 71 of the Act should be replaced by new sections based upon sections 156 to 166 of the BCA and that these new sections should apply to Ontario corporations only. Section 25 of the Act, which requires an Ontario corporation to keep a minute book, and section 29, which requires an Ontario corporation to keep a by-law book and confers a right to inspect the by-law book, should, in the Committee's opinion, be repealed. The content of sections 25 and 29 should be contained in the new sections recommended to replace sections 66, 66a, 69, 70 and 71. If these recommendations are implemented, the Act will then provide that an Ontario corporation may keep its records on computer or other form of electronic device. The Act will also provide that registers must be maintained in respect of the holders and the transfers of all securities issued by an Ontario corporation and that branch transfers may be maintained. All creditors of Ontario corporations, and not just depositors, debentureholders and holders of guaranteed certificates or receipts, will be empowered to examine certain records of the corporation and to make extracts therefrom within the principles of sections 162 and 163 of the BCA. The Committee would add to these recommendations the further recommendation that, in adapting the BCA principles to the Act, there should be a requirement that an Ontario corporation must obtain an order in council should it wish to maintain any records at an office other than its head office.[7] Such a requirement is needed in order to safeguard the other provisions of the Act with respect to the regulation and supervision of Ontario corporations.

14.03 The Committee does not consider it appropriate that the recommendations in paragraph 14.02 should extend to corporations which have their head offices in Ontario but are incorporated federally or under the laws of another province. An important part of the recommendations relates to matters affecting the internal affairs of a corporation and, in the Committee's opinion, such matters are more properly dealt with in the incorporating statute of the jurisdiction concerned. Accordingly, the Committee recommends that the new provisions recommended to replace sections 25, 29, 66, 66a and 71 of the Act should apply to Ontario corporations only. The Committee considers that the Registrar should have a discretionary power to require any federal or extra-provincial company registered under the Act to maintain in Ontario such records

covering its Ontario operations as the Registrar considers necessary. Accordingly, the Committee recommends the addition of such a section to the Act.

14.04 Section 67 of the Act provides that every registered corporation having its head office in Ontario must keep a register or registers of all securities held by the corporation. The Committee is unaware of any purpose to be served by this requirement of the Act. The annual statements filed with the Registrar would appear to contain whatever information he or his staff may require in connection with investments made by a corporation. The Act does not confer any right on a shareholder or creditor of a corporation to examine this register. There is no comparable requirement for such a register under the BCA. Accordingly, the Committee recommends that section 67 of the Act be repealed. It follows from this recommendation that section 68 of the Act should also be repealed.

14.05 Sections 69 and 70 of the Act contain provisions with respect to the books and records of a registered corporation which appeared to the Committee to be somewhat unusual. Section 69 (1) provides that the books used by an auditor, officer, collector or agent for verifying or recording money received for the corporation are the property of the corporation. The section implies that certain important books of account of a corporation might be prepared by and in the possession of an agent for the corporation who is not also an employee. While this may have been true in the case of some companies when the Act was first passed in 1912, it did not appear likely to the Committee that it would be true today. Section 70 of the Act deals with the situation where a former director, manager, auditor, officer, agent, collector, servant or employee of a corporation, or any other person, unlawfully retains possession of any accounts, books, money, securities, papers, matters or things that are the property of the corporation. In such circumstances, the corporation, any depositor or shareholder or the Registrar, may apply to the court for an order. The section makes provision for the imprisonment of any person unlawfully retaining possession of the corporation's property "for such period as the judge directs or until he complies with the direction of the order". This section would also seem to reflect the conditions applicable to the early loan corporations and building societies of Ontario which had few employees and often used the services of agents and volunteers. Research carried out for the Committee indicated that the language of section 70, which first appeared in the 1912 Act as section 108, bears a close similarity to a provision in the earlier Friendly Societies Act of the United Kingdom.[8] The Committee understands that loan and trust companies, as operated today, maintain both ownership and

possession of their books of record and account. They would appear to have, under the general law, the same rights as any other corporation to recover possession of their own property should it be removed from their possession. The Committee is unaware of any cases where resort to the provisions of sections 69 and 70 has been had. Accordingly, the Committee recommends that sections 69 and 70 be repealed.

14.06 **The Committee recommends that:**

(a) the provisions of the Act with respect to the books and records to be kept by an Ontario corporation should be changed so as to conform with the requirements imposed upon a business corporation by the BCA;

(b) consistent with recommendation (a) above, an Ontario corporation should be required to keep registers of the holders of, and registers of transfers with respect to, all securities issued by the corporation;

(c) the shareholders and creditors of an Ontario corporation should have the same rights to examine its books and records and to make extracts therefrom as are enjoyed by the shareholders and creditors of a business corporation under the BCA;

(d) a section similar to section 166 of the BCA, which provides that the court may order the rectification of certain records of a business corporation, should be added to the Act;

(e) the provisions of the Act respecting the maintenance of books and records; the right of shareholders and creditors to examine records and to make extracts therefrom; the right to obtain shareholders' lists; and the rectification of records, should apply to Ontario corporations only;

(f) a section should be added to the Act conferring discretionary power on the Registrar to require federal and extra-provincial corporations to maintain in Ontario such records concerning their Ontario operations as the Registrar considers necessary;

(g) sections 67 and 68 of the Act, which require certain registered corporations to keep registers of all securities held by such corporations and impose additional requirements in that connection, should be repealed; and

(h) sections 69 and 70 of the Act relating to the ownership by a registered corporation of certain books and records, the unlawful retention by third parties of such books and records and other property of the corporation, and related matters, should be repealed.

1. The Loan and Trust Corporations Amendment Act, 1973, S.O. 1973, c. 128, section 11.
2. The Act, section 2 (4).
3. See the Trust Companies Act, R.S.C. 1970, c. T-16, section 35 (1) and the Loan Companies Act, R.S.C. 1970, c. L-12, section 42 (1).
4. Trust Companies Act, R.S.C. 1970, c. T-16, section 35 (3). Loan Companies Act, R.S.C. 1970, c. L-12, section 42 (3).
5 Loan Companies Act, R.S.C. 1970, c. L-12, section 42 (1).
6. The BCA, sections 156 to 166.
7. See the Act, section 66 (4) which now requires an order in council.
8. Friendly Societies Act, 1875, Statutes of the United Kingdom, 38 and 39 Vic. c. 60, section 16 (9).

CHAPTER 15

Shares

15.01 The Committee approached this subject having previously considered the intermediary operations of loan and trust companies and having recognized the relationship and obvious importance of paid-in capital to a company's ability to exercise its intermediary powers effectively. One of the aims of the Committee in reviewing the sections of the Act relating to shares was to see whether any improvements could be made so that companies might raise capital more readily and free from any outmoded restrictions that might still be present in the Act. The Committee was aware in discussing this subject, however, that other policy considerations were present in the Act, such as the restrictions with respect to transfers of shares to, and the voting rights of, non-residents,[1] and the regulatory controls on increases or decreases in capital stock,[2] and that these considerations must be taken into account in recommending changes. It appeared to the Committee that changes to the share capital sections of the Act had occurred relatively recently when compared with The Corporations Act and the BCA. For example, although an oblique reference to "preference shares" was added to the Act in 1949,[3] it was not until 1970[4] that amendments were made to section 4 which clearly contemplated the division of a corporation's capital into several classes of shares and, in the case of preference shares, required the preferences to be provided for in the by-laws. Provision for the increase of capital by authorizing no par value shares came even later, being made by an amendment to the Act in 1973.[5] However, as the Act now stands, it still does not appear to be possible to incorporate an Ontario corporation with no par value shares in its authorized capital.[6] The trend of the legislative amendments to the share provisions of the Act has nonetheless been in the direction of closer uniformity with The Corporations Act and the BCA; no par value shares are now provided for; partly-paid shares are being phased out; and the provisions respecting preference shares have been made more explicit and tightened up. The questions for the Committee seemed to be, therefore, whether additional flexibility should be added to the Act in those areas where amendments had already occurred, and whether any of the more fundamental changes made in the BCA should be extended to Ontario corporations.

15.02 With respect to the first question, the Committee is aware of no reason why a corporation should not be incorporated in Ontario with no par value shares, either constituting the whole or part of its authorized

capital, and recommends, therefore, that the five year limitation in section 65 (1) be repealed. The Committee understands that it has been the policy of those responsible for the Act's administration not to permit the authorization of preference shares within a corporation's capital clause until it has been registered under the Act for a continuous period of five years. The Committee also recommends that this policy be discontinued. The preferences, rights, conditions, restrictions, limitations or prohibitions that may be attached to preference shares should be more broadly stated than as at present in section 4 (2) (d) of the Act, and the Committee recommends that the principles in section 27 (1) of the BCA be adopted instead. The Committee could find no justification for retaining the restrictions with respect to par value in section 50 of the Act and recommends that it be repealed so that an Ontario corporation may request whatever par value it desires. The Committee concurs with the 1970 amendment to the Act which prohibited the issue on or after June 30, 1970, of partly-paid shares.[7] The Committee understands that several Ontario corporations still have partly-paid shares outstanding but that these shares are to be paid up in full in stages as worked out in consultation with the Registrar. Since some corporations have partly-paid shares outstanding and a submission was received by the Committee on the point, the Committee recommends that section 9 (1) of the Act be amended by reintroducing the phrase "on or after the 30th day of June, 1970", which was deleted on consolidation of the Act in 1970, to remove any possible doubt with respect to corporations having outstanding partly-paid shares. Once partly-paid shares have been eliminated for all Ontario corporations, the sections of the Act referring or relating to partly-paid shares and to calls and forfeiture for non-payment, can be amended or in some instances repealed.[8] The Committee considers that the Act should contain more flexibility respecting the issue of shares. The Committee reviewed the provisions in the BCA respecting the issue of shares for a consideration consisting of property or services and concluded that Ontario corporations should be permitted to issue shares for property, but not for services, subject to a determination by the directors as to the value of property, as required by section 44 (5) of the BCA, and subject further to a requirement that the property must be an authorized investment within sections 150 (1) or 153 (1) of the Act. The Committee also considered section 9 (2) of the Act which prohibits the issue of shares at a discount and recommends that it be repealed and a new section based on the principles of section 45 of the BCA enacted in its place. The Committee also recommends that the payment of stock dividends by an Ontario corporation be expressly referred to in the Act.[9]

15.03 With respect to the second question, namely whether any of the

more fundamental changes made by the BCA should be extended to the Act, the Committee considered section 39 of the BCA relating to the power of a business corporation to purchase its common shares. Section 39 (2) provides:

> "(2) Where authorized in its articles and subject to any restrictions contained therein, a corporation may purchase any of its issued common shares."[10]

The Committee considered that, as long as this new statutory right were not used so as to reduce an Ontario corporation's capital and reserve to an amount that would place the corporation in contravention of sections 82 or 90,[11] the right to purchase issued common shares should be afforded to Ontario corporations. Grant of the right would of course be discretionary in that it requires authorization in the corporation's letters patent or supplementary letters patent. Exercise of the right would also be subject to the solvency test provided for in section 39 (3) of the BCA. The Committee recommends that the Act be amended by adding to section 65 (12) the additional power whereby an Ontario corporation, where authorized by its letters patent or supplementary letters patent and subject to any restrictions therein, may purchase any of its issued common shares, with the proviso that such power should follow the principles in section 39 of the BCA and any exercise thereof should be subject to the additional requirement that the unimpaired capital and reserve of the corporation not be reduced to an amount that would place the corporation in contravention of sections 82 or 90. It would follow from this recommendation that sections 115 (3) and 117 (3) of the Act are no longer required and should be repealed.

15.04 It was pointed out in paragraph 12.03 that the capital clause of an Ontario corporation is contained in its by-laws and that increases or decreases or alterations in share capital are effected by amending by-law passed in accordance with section 65 of the Act and confirmed by order in council under section 65 (8). Section 65 does not refer to the issue of supplementary letters patent nor are such letters patent issued as a matter of policy. The Committee noted that: (a) under section 65 (5) a copy of the by-law must be delivered to the Registrar at least one month before the by-law is passed; (b) under section 65 (6) the holders of at least 50% of the issued shares of the corporation for the time being carrying voting rights must be present in person or represented by proxy at the general meeting of shareholders called to confirm the passing of the by-law; and (c) under section 65 (8) the Lieutenant Governor in Council may grant his confirmation of the by-law if he is satisfied of the bona fide character of the changes provided for in the by-law, "unless it appears that the confirmation of the by-law would not be in the public

interest". On the basic question whether changes in authorized capital should continue to be discretionary, the Committee concluded affirmatively that they should be, but recommends that some amendments be made to section 65. The Committee recommends that: (a) changes in the capital clause be effected by the issue of supplementary letters patent; (b) the requirement for the holders of at least 50% of the issued voting shares to be present or represented at the shareholders' meeting and the requirement for a confirmatory order in council be dropped; (c) application for supplementary letters patent be approved by a "special resolution"; (d) subsection (5) of section 65 be retained, "special resolution" being substituted for "by-law" wherever the latter term appears therein; (e) the Minister have a discretion with respect to the grant of supplementary letters patent; and (f) there be no appeal from an exercise by the Minister of his discretion.

15.05 The Committee reviewed sections 54 to 57 of the Act relating to transfers of shares to, and the exercise of voting rights by, non-residents. These sections were added to the Act in 1970 and 1972[12] and followed earlier amendments of a similar nature to the Federal Acts. The sections are quite technical in nature and the Committee does not consider that it should make any recommendations with respect to the detail of the sections. The Committee understands that the principle of sections 54 to 57 is to impose statutory restrictions upon transfers of shares of Ontario corporations to non-residents and upon the exercise by non-residents of the voting rights attached to such shares. The Committee concurs with this principle. Sections 60, 62 and 63 of the Act, which deal with share transfers generally, are based on the principle that entry in the books of the corporation is necessary to effect a legal transfer. The Committee noted that the transfer of "securities" of business corporations is governed by sections 63 to 97 of the BCA which are designed to make the securities of business corporations freely transferable. While there appeared to the Committee to be some incompatibility between the free transferability principle of the BCA provisions and the restrictions on transfer in sections 55, 57 and 58 of the Act, the Committee was advised of the fact that under the BCA provisions, certain corporations that offer their shares to the public may, in limited circumstances, impose restrictions on the transfer of their shares and that the issuer's duty to register a transfer of shares is qualified by reference to the restrictions so imposed.[13] The Committee concluded therefore and recommends that the provisions with respect to the transfer of securities of business corporations, as set forth in sections 63 to 97 of the BCA, should be added to the Act and made applicable to transfers of the shares (but not other securities) of Ontario corporations, subject to the proviso that the duty of an Ontario corporation to register a transfer should, in addition

to the existing requirements of the BCA provisions, be qualified by reference to the provisions of sections 54 to 59 of the Act and to section 60 of the Act relating to partly-paid shares.

15.06 The Committee understands that, except for section 58, there are no controls in the Act on the transfer of shares of an Ontario corporation to a Canadian resident. Section 58 of the Act provides that:

> "No transfers or issue of shares of a corporation shall be entered in the books maintained under section 66 until thirty days after notice thereof has been deposited with the Registrar, if,
>
> (a) the transfer or issue relates to 10 per cent or more of the issued shares of the corporation for the time being enjoying voting rights; or
>
> (b) the directors have reason to believe that the transfer or issue would result in a majority of the issued shares of the corporation for the time being enjoying voting rights being beneficially owned by any one person."

This section applies to transfers and issues of shares to residents of Canada as well as to non-residents. The Committee noted that the section does not confer any power on the Registrar to prohibit the transfer or issue of shares and the apparent purpose of the section would seem to be to give the Registrar advance notice of pending transfers and issues of shares of a significant nature. The Committee understands that there are somewhat tighter provisions in other loan and trust legislation.[14] The Committee has concluded that it does not wish to recommend any changes to the Act in this connection but does wish to record the fact that it would be a matter of concern to the Committee should control of Ontario corporations become concentrated within a relatively few corporate groups.

15.07 In the Committee's opinion, the terminology in the Act relating to shares should be updated. The Committee is aware of no need to retain the adjective "permanent" when referring to capital stock in the Act.[15] This appears to be a survival of the building society legislation which distinguished between the terminating and permanent shares of a society. The Committee also recommends that the BCA terminology which distinguishes between "shares" and "special shares" should be adopted in place of the current distinction in the Act between "common shares" and "preference shares". The principles of sections 49 to 52 of the BCA respecting share certificates should also, in the Committee's opinion, be substituted for section 61 of the Act.

15.08 **The Committee recommends that:**

(a) Ontario corporations be permitted to be incorporated with no par

value shares or preference shares in their authorized capital;

(b) the principles of the BCA respecting the preferences, rights, conditions, restrictions or prohibitions that may be attached to preference shares be adopted in the Act;

(c) section 9 (1) of the Act be amended by introducing after "issued" in the first line, the phrase "on or after the 30th day of June, 1970";

(d) Ontario corporations be permitted to issue shares for a consideration consisting of property provided that such property would otherwise constitute an authorized investment under sections 150 (1) and 153 (1) of the Act;

(e) section 9 (2) of the Act be amended so that Ontario corporations may issue shares at a discount within the principles of section 45 of the BCA;

(f) the Act be amended so that Ontario corporations may obtain the right to purchase their issued common shares;

(g) section 65 of the Act be amended so that changes in the authorized capital of an Ontario corporation will be effected by the issue, in the discretion of the Minister, of supplementary letters patent, the application for which has been previously approved by special resolution, and that there be no appeal from any exercise by the Minister of his discretion;

(h) the Act be amended by introducing new provisions based upon sections 63 to 97 of the BCA insofar only as those sections relate to the shares of an Ontario corporation, subject to qualification being made to preserve the existing provisions of the Act respecting transfers within sections 55, 58 and 60 of the Act;

(i) use of the term "permanent" throughout the Act with reference to shares be discontinued as being no longer meaningful to the shares of registered corporations;

(j) the BCA terminology which distinguishes between "shares" and "special shares" be adopted for the Act; and

(k) the principles with respect to share certificates as contained in sections 49 to 52 of the BCA be adopted in the Act.

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1. The Act, sections 54 to 59.
2. The Act, section 65.
3. The Loan and Trust Corporations Act, 1949, S.O. 1949, c. 52, section 14.
4. The Loan and Trust Corporations Amendment Act, 1970 (No. 2), S.O. 1970, c. 129, section 3 (1).
5. The Loan and Trust Corporations Amendment Act, 1973, S.O. 1973, c. 128, sections 9 and 10.

6. The Act, sections 3 (3) and 8 (1).
7. The BCA does not permit a business corporation to issue partly-paid shares. See section 44 (4).
8. For references to partly-paid shares in the Act, see sections 1 (j), 8 (1), 18 (2) (a), 23, 33 (a), 35 (2), 47, 48, 52, 53, 60, 65 (3) and 78 (2) (c.).
9. See, for example, section 155 of the BCA.
10. The BCA, section 39 (2).
11. For the application of this requirement to redemption or purchase for cancellation of issued preference shares, see section 65 (13) of the Act.
12. The Loan and Trust Corporations Amendment Act, 1970 (No. 1), S.O. 1970, c. 84. The Loan and Trust Corporations Amendment Act, 1972, S.O. 1972, c. 101, section 4.
13. See sections 47 (2) and 92 (1) (e) of the BCA.
14. See, for example, section 64 of the Alberta Act. See also section 5.1 of the Federal Acts.
15. See, for example, sections 3 (3) and 137 (1) 3 of the Act.

CHAPTER 16

Shareholders

16.01 The Committee considered the matter of shareholders' rights and in that connection, examined the provisions of the Act and comparisons suggested by the BCA. Without attempting to summarize all of the rights conferred by the Act, it is sufficient for the purposes of this Chapter to mention rights given to shareholders of Ontario corporations in respect to annual and general meetings of shareholders;[1] the requisitioning of meetings;[2] voting at meetings;[3] receipt of the financial statements and auditor's report;[4] and, in the case of shareholders of all corporations, rights in respect of requisitioning an audit by an accountant appointed by the Registrar[5] or a special examination and audit by a person appointed by the Minister.[6] Some of these rights are granted to shareholders of business corporations by the BCA, but, and this is the significance of the comparison, the BCA goes considerably further in granting rights to shareholders than the Act does. Under the BCA, a shareholder may, for example and subject to certain conditions, (a) bring an action in a representative capacity suing on behalf of the corporation;[7] (b) apply to the court for an order requiring the directors to call a general meeting of shareholders;[8] (c) apply to the court for an order appointing an inspector to investigate the affairs and management of the corporation and to audit its accounts;[9] (d) apply to the court for an order directing the corporation, or its directors, officers or employees, to comply with any provision of the Act, the articles or by-laws of the corporation.[10] Some of these rights were new under the BCA, others simply amended existing provisions of The Corporations Act, and in all cases mentioned above, the new or amended rights resulted from recommendations in the 1967 interim report of the Select Committee.[11] The question of the rights of shareholders, whether as minority shareholders or as part of the majority, was an important matter considered in the 1967 report and many of its recommendations were adopted by the BCA. This raised for the Committee the important question: should these rights be given to the shareholders of loan and trust corporations?

16.02 With respect to such matters as the length of notice that should be required in order to call a shareholders' meeting, the right of a shareholder to raise any matter relevant to the affairs and business of a corporation at the annual meeting, and the right of the shareholders to remove a director from office prior to the expiry of his term, the Committee considered that the Act should follow the approach adopted by the BCA. These and other similar matters will be referred to again in

paragraphs 16.04 and 16.05 where the Committee makes specific recommendations for amendments to the Act. With respect to more substantive matters, however, such as the right to commence derivative actions, or to apply to the court for an order directing compliance with provisions of the BCA or the corporation's articles or by-laws, it appeared to the Committee that a basic question arose as to whether it would be desirable for shareholders of regulated loan and trust companies to have such rights. These rights are dependent upon court order and seem to raise the issue of the extent to which the court should become involved in deciding questions of compliance or non-compliance with the Act, or in ordering a special investigation and audit of a loan or trust corporation to be carried out, when responsibilities for such matters have already been placed upon the Registrar by the Act itself.[12] The question has already been considered in relation to trust companies and to proposals for amendment to the Act by Hughes J. in the Atlantic Report.[13] At page 1651 of the report, he made the following comments with respect to the need to protect directors of a trust company from derivative suits:

> "The second [observation concerning sections of the Act dealing with directors] arises from the necessity of protecting the directors of a trust company from the type of action contemplated by section 87 of the proposed Business Corporations Act 1968, [now section 99] as I have already suggested to be desirable in the case of another type of intermediary, the finance company. In the case contemplated by section 41, subsection 2 thereof gives the necessary protection. Generally speaking, however, the provisions of Recommendation X made with respect to finance companies should be repeated in the case of trust companies, and for the same reasons stated with even greater emphasis, since the position of trust companies, fulfilling a purpose more closely associated with public need than that of the ordinary commercial company, and subject to greater scrutiny and regulation by government agencies, requires, first, the absolute protection of responsible directors, from vexatious legal proceedings, and second, the certainty that such proceedings, with their unpredictable result, should not be at cross-purposes with the policy of that regulation."[14]

Hughes J. went on to make recommendations, should the Legislature consider it wise to make the statutory derivative suit available to the shareholders of trust companies, and the last two of his recommendations were as follows:

> "3. In any such action, notice, security for costs and costs should be in the discretion of the Court.
>
> 4. Indemnification by a trust company of a director or officer

against whom such an action has been brought by a shareholder of such a company in a representative capacity on behalf of the company should be a question for its shareholders other than such director or officer."[15]

These comments and recommendations were examined by the Committee both with respect to their application to loan and trust companies under the Act and in the light of the apparent infrequent use made of section 99 since it came into force on January 1, 1971. It did not appear to the Committee that section 99 had proved thus far to be a source of harassing or vexatious proceedings against the directors or officers of business corporations. The Committee also did not consider that it would be detrimental to the purposes of the Act, or that it would detract from the role or authority of the Registrar to carry out his regulatory functions, if shareholders were given a statutory right to apply to the court for an order permitting them to maintain representative actions.

Section 99 (1) of the BCA provides as follows:

> "Subject to subsection 2, a shareholder of a corporation may maintain an action in a representative capacity for himself and all other shareholders of the corporation suing for and on behalf of the corporation to enforce any right, duty or obligation owed to the corporation under this Act or under any other statute or rule of law or equity that could be enforced by the corporation itself, or to obtain damages for any breach of any such right, duty or obligation."[16]

The Committee has concluded that this right should also be conferred on the shareholders of Ontario corporations and does not consider that further safeguards, in addition to those already provided for in section 99 of the BCA, are required. Accordingly, the Committee recommends that the Act be amended by adding thereto a new section in the same terms as section 99 of the BCA. It follows from this recommendation that a definition of the term "court" should be added to section 1 of the Act.

16.03 The Committee went on to consider the rights conferred upon shareholders of business corporations by sections 186, 187 and 261 (1) of the BCA. Under section 186, a shareholder of a corporation may apply to the court for an order appointing an inspector to investigate the affairs and management of the corporation and to audit its accounts and records.[17] The order may extend to affiliates of the corporation. Section 187 (1) of the BCA provides that a corporation may, by resolution passed at an annual meeting of shareholders or a general meeting of shareholders called for that purpose, appoint an inspector to investigate its affairs and management. Section 261 (1) of the BCA provides, in effect, that where

a corporation or a director, officer or employee of a corporation does not comply with any provision of the BCA, the articles or the by-laws of the corporation, a shareholder or a creditor of the corporation may apply to the court for an order directing the corporation, director, officer or employee, to comply with such provision.[18] The Committee noted that under sections 186 (1) and 261 (1) the application is made to the court, which has a discretion as to the granting of the order and the terms thereof. There appeared to be no equivalent to section 261 (1) in the Act and, with respect to section 186 (1), section 123 of the Act appeared to provide the closest analogy. Section 123 (1) of the Act provides that:

> "The Registrar or any person authorized under his hand and seal may, with the approval of the Minister, at any time within business hours, examine the books, vouchers, securities and documents of a corporation, and any officer or person in charge, possession, custody or control of the books, vouchers, securities or documents refusing or neglecting to afford such examination is guilty of an offence, and the corporation, if registered, is liable to have its registry suspended."

and section 123 (3) provides that:

> "Where,
>
> (a) a corporation is three months in default in the delivery of the annual statement required by section 168; or
>
> (b) for eighteen consecutive months there has been no audit of the books and accounts of the corporation; or
>
> (c) there is filed with the Registrar a requisition for audit bearing the signatures and addresses of at least twenty-five shareholders of the corporation holding shares upon which not less than $10,000 in the aggregate has been paid in, alleging specific fraudulent or illegal acts or repudiation of contracts or alleging that the accounts of the corporation have been materially and wilfully falsified and accompanied by a deposit of $1,000 or such other sum as the Registrar may fix as security for the cost of the audit,
>
> the Registrar may appoint an accountant who shall under his direction make a special audit of the books, accounts and securities of the corporation and make to the Registrar a written report thereon."

It appeared significant to the Committee that under section 123 (1) the Registrar or his appointee makes the examination, and that under section 123 (3) it is to the Registrar that the shareholders make their application. The Committee considers that it would be undesirable to

introduce sections 186 and 187 into the Act since such a change might frustrate the purposes of the Act and seems to the Committee to be inconsistent with the notion of an industry regulated by statute. No doubt, as the Act now stands, any shareholder could lodge a complaint with the Registrar who, if he considered that the complaint had merit, would take it up with the corporation concerned and, in the absence of a satisfactory explanation, might proceed under section 123 (1). With regard to section 261 (1), however, the Committee considers that it would present a further safeguard if, in addition to the regulatory controls under the Act, a shareholder or a creditor had a statutory right to seek an order requiring a corporation, or a director, officer or employee of a corporation to comply with any provision of the Act, the charter or the by-laws of the corporation. The Committee considers, however, that the application should be made to the Registrar and not to the court, that the Registrar should make his decision in writing, and that an appeal therefrom should lie to The Commercial Registration Appeal Tribunal. The Committee therefore recommends that a new section be added to the Act based on section 261 (1) of the BCA and providing that the application shall be made to the Registrar.

16.04 The Committee considered the matter of the shareholders' rights in regard to meetings of shareholders and concluded that amendments to the Act were required. With respect to the annual meeting, the Committee recommends that section 19 should be amended by adding thereto a sentence stating "At the annual meeting any shareholder shall have an opportunity to raise any matter relevant to the affairs and business of the corporation."[19] The minimum notice to be given of a shareholders' meeting should be increased from ten days to 21 days[20] and there should be a statutory limitation upon the maximum notice that may be given. The Committee considers that the 50 day limit imposed by the BCA[21] is appropriate for the Act and recommends that it be adopted. Provision should be made in the Act for the minimum notice period to remain at ten days for any registered Ontario corporation that has less than 15 shareholders. Section 75 (5) of the Act, which relates to the sending of the financial statements and auditor's report to the shareholders, should be similarly amended to provide for mailing 21 days or more before the date of the annual meeting, with the same maximum of 50 days and a similar exemption for a registered Ontario corporation having less than 15 shareholders. Section 22 of the Act relating to record dates should be amended so as to follow the principles of section 112 (1) of the BCA. The Act should provide that persons who hold equity shares of an Ontario corporation carrying at least five per cent of the voting rights attached to all equity shares of the corporation outstanding may requisition the directors to:

"(a) give to the shareholders entitled to notice of the next meeting of shareholders notice of any resolution that may properly be moved and is intended to be moved at that meeting; or

(b) circulate to the shareholders entitled to vote at the next meeting of shareholders a statement of not more than 1,000 words with respect to the matter referred to in any proposed resolution or with respect to the business to be dealt with at that meeting."[22]

The Committee recommends that a section based on section 102 of the BCA (from which the foregoing excerpt has been taken) should be added to the Act. Registered corporations having less than 15 shareholders should be exempt from the provision. The Committee noted that section 102 (5) makes provision for an application to the court and the Committee considers that a right to apply to the court in the circumstances contemplated by section 102 of the BCA would be appropriate for Ontario corporations as well.

16.05 The Committee considered whether shareholders of Ontario corporations should be permitted to act by means of signed resolution or by-law in lieu of action taken at a meeting.[23] The Committee considers that such a right would not be desirable for loan or trust corporations and therefore recommends that no provision to that effect be added to the Act. The Committee also considered section 20, subsections (2) to (6) of the Act which provide for the requisitioning of shareholders' meetings. Section 20, subsections (2), (3) and (4) provide that:

"(2) Shareholders holding not less than 10 per cent of the issued shares of a corporation carrying the right to vote at the meeting may request the directors to call a general meeting of the shareholders for any purpose that is connected with the affairs of the corporation and that is not inconsistent with this Act.

(3) The requisition shall state the general nature of the business to be presented at the meeting and shall be signed by the requisitionists and deposited at the head office of the corporation, and may consist of several documents in like form signed by one or more requisitionists.

(4) Upon deposit of the requisition, the directors shall call forthwith a general meeting of the shareholders for the transaction of the business stated in the requisition."

These provisions are virtually the same as subsections (1), (2) and (3) of section 109 of the BCA, except that under the BCA the percentage of shares that must be held by the requisitionists has been reduced to five per cent. Section 109 of the BCA also goes on to provide that any of the requisitionists may call the meeting if the directors do not do so as required by section 109, and provides that the meeting shall be called as nearly

as possible in the same manner as meetings of shareholders are called under the by-laws. In the same section conditional provision is made for payment of certain expenses of the requisitionists. The Committeee recommends that section 20 of the Act be amended so as to include the provisions of subsections (4), (5) and (6) of section 109 of the BCA. The Committee also recommends that a new section be added to the Act incorporating the provisions of section 110 of the BCA, which authorizes any shareholder of a business corporation to make application to the court for an order requisitioning a meeting of its shareholders.[24] In making this recommendation, the Committee adds the qualification that on any such application the court should be satisfied that it is made in good faith and that it is prima facie in the interests of the corporation and the holders of its securities, not just its shareholders, that the meeting be held.

16.06 With regard to certain other rights of shareholders, recommendations have already been made in paragraph 13.09 that the shareholders, by majority vote, should have a statutory right to remove any director before the expiry of his term of office. Mention was also made in paragraph 13.09 that the remuneration of directors of Ontario corporations should, under the new Act, be governed by the principles of section 22 of the BCA. The Committee considered section 23 of the Act regarding the voting rights of shareholders and noted that it limits the holder of a share to one vote per share. The Committee recommends that this provision be retained. The Committee noted that the Act does not appear to contain any provision comparable to section 104 of the BCA which provides as follows:

> "A shareholder of a corporation as such is not answerable or responsible for any act, default, obligation or liability of the corporation, or for any engagement, claim, payment, loss, injury, transaction, matter or thing relating to or connected with the corporation."

The Committee recommends that a similar provision, applicable to the shareholders of Ontario corporations, be added to the Act. Such provision should preserve the liability of the shareholder to the corporation, however, in respect to any amounts unpaid on his shares of the corporation.[25]

16.07 **The Committee recommends that:**

(a) a shareholder of an Ontario corporation be empowered to apply to the court for an order permitting him to commence a representative action on behalf of the corporation to enforce any right, duty or obligation owed to the corporation under the Act or under any other statute or rule of law or equity that could be enforced by the

corporation itself, or to obtain damages for any breach of any such right, duty or obligation, and that the provisions of section 99 of the BCA with respect to such actions be incorporated in the Act;

(b) the provisions of sections 186 and 187 of the BCA with respect to the appointment of an inspector to investigate the affairs and management of a corporation not be adopted in the Act;

(c) a new section be added to the Act whereby a shareholder or a creditor of an Ontario corporation may apply to the Registrar for an order directing the corporation, or a director, officer or employee of the corporation to comply with any provision of the Act, the letters patent or supplementary letters patent or by-laws of the corporation;

(d) a shareholder of an Ontario corporation be permitted under the Act to raise, at an annual meeting, any matter relevant to the affairs and business of the corporation;

(e) the minimum notice for shareholders' meetings be increased from ten to 21 days, the maximum notice be fixed by the Act at 50 days, and that these provisions also apply with respect to the mailing of financial statements and the auditor's report;

(f) with regard to recommendation (e), the minimum notice period for a registered Ontario corporation having less than 15 shareholders should remain at ten days;

(g) the provisions of section 22 of the Act with respect to the fixing of record dates be changed to conform with the principles of section 112 (1) of the BCA;

(h) a new section be added to the Act based on section 102 of the BCA requiring the directors to give notice to the shareholders of any resolution that may properly be moved and is intended to be moved at a meeting of the shareholders, or to circulate to the shareholders entitled to vote at the next meeting of shareholders a statement of not more than 1,000 words with respect to the subject matter of a proposed resolution or with respect to the business to be dealt with at that meeting;

(i) the recommendation referred to in (h) should not apply to Ontario corporations having less than 15 shareholders;

(j) shareholders of Ontario corporations should not be afforded the rights contained in section 23 (2) and (3) of the BCA whereby shareholders may act by means of an unanimously signed resolution or may confirm a by-law passed by the directors by unanimously signed written confirmation without, in either case, holding a meeting;

(k) section 20 of the Act be amended so as to include the provisions of subsections (4), (5) and (6) of section 109 of the BCA;

(l) a new section be added to the Act authorizing any shareholder of an Ontario corporation to apply to the court for an order requisitioning the holding of a meeting of shareholders, subject to the proviso that in making the order the court should be satisfied that the application has been made in good faith and that it is prima facie in the interests of the corporation and the holders of its securities that the meeting be held;

(m) there be no change in section 23 of the Act which provides that, subject to the conditions, restrictions, limitations or prohibitions applicable to any outstanding preference shares, the holder of each share in the capital of an Ontario corporation shall be entitled to one vote per share; and

(n) a new section relating to the liability of shareholders of Ontario corporations and based upon section 104 of the BCA be added to the Act.

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1. The Act, sections 19 and 20.
2. The Act, section 20 (2), (3) and (4).
3. The Act, section 23.
4. The Act, section 75 (5).
5. The Act, section 123 (3) (c).
6. The Act, section 124 (1).
7. The BCA, section 99.
8. The BCA, section 110.
9. The BCA, section 186. The order may include, or be confined to, any affiliate of the corporation.
10. The BCA, section 261.
11. 1967 Interim Report of the Select Committee on Company Law tabled in the Legislative Assembly of the Province of Ontario.
12. See, for example, sections 135 (7) and 128 (1) of the Act. For an example of a section of the Act where a shareholder may apply to the court for an order, see section 70.
13. Atlantic Report, Vol. 3, pp. 1510-12, 1620-25 and 1650-51.
14. Atlantic Report, Vol. 3, p. 1651.
15. Atlantic Report, Vol. 3, p. 1651. Note that part of the third recommendation has received recognition in the BCA. See the BCA, section 99 (3) which requires the applicant to give at least seven days notice of the application to the corporation. Under section 87 (3) of Bill 125, the application could be made ex parte.
16. The BCA, section 99 (1).

17. Section 186 (1) of the BCA provides as follows:
"Upon application by a shareholder of a corporation, the court, if satisfied that the application is made in good faith and that it is prima facie in the interests of the corporation or the holders of its securities to do so, may make an order, upon such terms as to the costs of the investigation or audit or otherwise as to the court seems fit, appointing an inspector to investigate the affairs and management of the corporation or any affiliate of the corporation, or both, and to audit the accounts and records of the corporation or any affiliate thereof named in the order."
18. Section 261 (1) of the BCA provides as follows:
"Where a corporation or a director, officer or employee of a corporation does not comply with any provision of this Act, the articles or the by-laws of the corporation, a shareholder or a creditor of the corporation, notwithstanding the imposition of any penalty in respect of such non-compliance and in addition to any other rights he may have, may apply to the court for an order directing the corporation, director, officer or employee, as the case may be, to comply with such provision and upon such an application the court may make such order or such other order as the court thinks fit."
19. The BCA, section 107 (1).
20. The Act, sections 19 (2) and 20 (5).
21. The BCA, section 106 (1).
22. The BCA, section 102 (1).
23. See section 23 (2) and (3) of the BCA.
24. Section 110 of the BCA provides as follows:
"Notwithstanding section 109, upon application by a shareholder of a corporation, the court, if satisfied that the application is made in good faith and that it is prima facie in the interests of the corporation or its shareholders that the meeting be held on requisition, may make an order, upon such terms as to security for the costs of holding the meeting or otherwise as to the court seem fit, requiring the directors to call a general meeting of the shareholders for any purpose that is connected with the affairs of the corporation and that is not inconsistent with this Act."
25. See The Corporations Act, R.S.O. 1960, c. 71, section 55 (1).

CHAPTER 17

Regulation and Examination

17.01 This chapter and the next deal with matters concerning the ongoing regulation and supervision of loan and trust companies in Ontario. Chapter 17 deals primarily with the companies' statutory obligations to submit periodic returns and the Registrar's obligation to carry out annual examinations. Chapter 18 deals with examinations by a company's auditors and their reports to the shareholders and the Registrar. The Committee considered these matters to be of great importance and, consequently, they were thoroughly reviewed and discussed. The principal sections of the Act of an ongoing regulatory nature appear to be section 168 relating to the filing of annual statements with the Registrar, section 126 relating to an annual examination by the Registrar, and section 122 relating to the annual report by the Registrar to the Minister showing particulars of the business of each corporation as ascertained from the annual statements filed with him and the examinations which he has carried out. In addition to the foregoing, the Act contains requirements concerning the following: the completion and filing with the Registrar of quarterly, semi-annual and annual returns in relation to intermediary operations;[1] the carrying out of special examinations with the Minister's approval or of his own motion where unusual circumstances exist;[2] the suspension or cancellation of a corporation's certificate of registry by the Lieutenant Governor in Council under section 128 of the Act where the corporation's assets are insufficient to justify its continuance in business, or by the Registrar under section 138 of the Act where, among other things, a corporation is insolvent, has failed to pay its obligations, or has wilfully contravened any of the provisions of the Act. In the case of Ontario corporations, new provisions were added to the Act in 1970 to empower the Registrar, when acting on the authority of an order in council, to take possession and control of the assets of an Ontario corporation in financial difficulty and to carry on its business with a view to its rehabilitation.[3] As this summary shows, very considerable regulatory powers are conferred by the Act on the Registrar and the Lieutenant Governor in Council, no doubt principally with a view to providing some added protection to those members of the public who have deposited funds with, or invested moneys in the short-term securities of, a registered corporation, and who, as previously mentioned in paragraph 5.05, do not enjoy the customary protection of a prospectus.

17.02 Since April, 1967, additional protection to loan and trust com-

pany depositors and to investors in their short-term debt securities has been afforded by deposit insurance. Section 23 (1) of The Ontario Deposit Insurance Corporation Act provides that:

> "23 (1) No loan corporation or trust company registered under The Loan and Trust Corporations Act shall, after the 30th day of June, 1967, accept, receive or issue deposits unless it holds a certificate or policy of deposit insurance issued by The Canada Deposit Insurance Corporation or unless its deposits are insured in some other manner approved by the Lieutenant Governor in Council."[4]

Under present arrangements, the practical effect of this section is that registered corporations that accept, receive or issue deposits must hold a policy of deposit insurance issued by The Canada Deposit Insurance Corporation (hereinafter referred to as the "CDIC"). Under such a policy, CDIC insures each deposit with a member institution except (a) a deposit that is not payable in Canada or in Canadian currency; (b) a deposit in respect of which Her Majesty in right of Canada would be a preferred claimant; and (c) so much of any one 'deposit' as exceeds $20,000.[5] Further protection for depositors is provided by the provisions of the Canada Deposit Insurance Corporation Act[6] which requires each member institution to be examined annually. The examination of federally incorporated loan and trust corporations is carried out by the federal Superintendent of Insurance and the examination of Ontario incorporated loan and trust companies is carried out by the Registrar through agreement with CDIC. Under the Canada Deposit Insurance Corporation Act, the person making the examination is required to report to CDIC after his examination

> "whether or not, in his opinion, there has been any change in the circumstances of the member institution that might materially affect the position of the Corporation [CDIC] as an insurer and particularly, without limiting the generality of the foregoing, whether or not, in his opinion,
>
> (a) the returns made by the member institution and on which its premiums were based are correct;
>
> (b) the operations of the member institution are being conducted in accordance with sound business and financial practices; and
>
> (c) the member institution is in a satisfactory financial condition."[7]

The Canada Deposit Insurance Corporation Act goes on to provide that CDIC may terminate a policy of deposit insurance issued to a provincially incorporated loan or trust company where it has been advised that such company is following unsound business or financial practices or is in breach of any conditions of its policy of insurance and that such matters

have not been remedied by the company within the prescribed time limits. In case of any insolvency, CDIC is also granted discretionary power to "initiate, and take any measures or proceedings that a creditor of the member institution may initiate or take under law to preserve the assets of the member institution, to have it wound up or to petition for a receiving order under the Bankruptcy Act."[8] The Committee concluded from its review of these provisions that very substantial powers of regulation had been bestowed upon CDIC, especially having regard to the obviously serious consequences that would flow from any termination of a member institution's policy of deposit insurance, and that important responsibilities of examination had devolved upon the Registrar under the arrangements just described.[9] In performing his duties, the Registrar is now responsible to two superiors, that is, to the Minister in respect to examinations made under the Act, and to CDIC in respect to examinations made under the deposit insurance arrangements. The Committee does not consider that it is within its terms of reference to make any recommendations with respect to these relatively new additional responsibilities of the Registrar and, having noted them, would simply observe that duplication of regulation of Ontario corporations has been avoided by the arrangements worked out with the federal authorities; a desirable result in the Committee's opinion.

17.03 The Committee discussed the general principles underlying the examination of registered corporations under the Act. While, in the Committee's opinion, examination provides an additional level of protection to the public, neither it nor the other provisions of the Act should be so construed as to constitute any representation by the Government of Ontario, the Minister or the Registrar as to the solvency or financial standing of any corporation registered under the Act. The Committee notes section 145 of the Act which provides that:

> "145. (1) No corporation shall, under the penalty of becoming disentitled to registry or of having its registry suspended or cancelled, make, print, publish, circulate, authorize or be a party or privy to the making, printing, publishing or circulating of any statement or representation that its solvency or financial standing is vouched for by the Registrar or that the publication of its statement in his report is a warranty or representation of the solvency of the corporation or of the truth or accuracy of the statement in any particular.
>
> (2) Any director, auditor, officer, servant, employee or agent of a corporation who makes or uses or authorizes or is party or privy to the making or using of any such statement or representation is guilty of an offence."

On comparison of this section with sections 202 and 203 of the Alberta

Act, the Committee noted that the Alberta Act also specifically refers to the Government and the Minister. The Committee therefore recommends that section 145 be amended to provide that "no corporation shall . . . make, print, publish, circulate, . . . any statement or representation that its solvency or financial standing is vouched for by the Government of Ontario, the Minister or by the Registrar . . .".

17.04 No submissions were received by the Committee from the industry or from the Registrar requesting substantive changes in sections 118 to 132 of the Act relating to the Registrar and to the examination of registered corporations. The Committee inquired with respect to the matter of maintaining a sense of distance between those responsible for administering the Act and representatives of the industry and was advised by the Registrar that guidelines had already been circulated among his staff who were well aware of the importance of maintaining independent, impartial regulation of the industry. The Committee was fully satisfied by the answers given to its inquiries in this connection and simply refers to the matter in this report in order to signify the importance that it attaches to it. Although the Committee expresses no concern, it does consider that section 5 of the Insurance Act[10] would be a useful addition to the Act, and therefore recommends that a new section be added to the Act as follows:

> "Neither the Registrar, the Assistant Registrar, nor any examiner of a registered corporation who is responsible to the Registrar, shall be interested as a shareholder, directly or indirectly, in any registered corporation."

The Committee noted that sections 123 (1) and 124 of the Act appear to be deficient in that they do not indicate what action may be taken as a result of a report made thereunder. Should such a report indicate, in the opinion of the Registrar or the Minister as the case may be, that the assets of the corporation are insufficient to justify its continuance in business, the Act should provide for suspension or cancellation of the corporation's registry by order in council after following the steps described in section 128 (1) and (2), as appropriate. The Committee therefore recommends that sections 123 and 124 be amended accordingly. The Committee also noted that the Registrar's right of inspection under sections 123 (1) and 126 (3) of the Act might not extend to all records in the possession of the corporation concerned, and the Committee recommends that sections 123 (1) and 126 (3) be amended so as to remove any possible doubt as to the Registrar's right to inspect or examine any books or records possessed by a registered corporation. The Committee considers that some rearrangement of the sections in this part of the Act should be made in the new Act. Section 127, which relates to inquiries

by the Registrar, should more properly come after section 128 and not before it; and subsections (6) and (7) of section 124 appeared to the Committee to belong to the section of the Act dealing with returns and not as subsections of section 124.

17.05 The examination of loan and trust companies carrying on business in Ontario was a matter of prime concern to the Committee. At the request of the Committee, the Registrar prepared for its review a memorandum containing details on the organization of his office, the staff at his disposal for purposes of the Act, and the frequency and nature of loan and trust company examinations. As the memorandum indicated, the Registrar has responsibilities under a number of Acts, including his responsibilities as Superintendent of Insurance under the Insurance Act,[11] and consequently his time, as well as that of his most senior assistants, is only partly devoted to the supervision of loan and trust companies. The Registrar's staff includes, however, an examination staff of nine who, except for the Chief Examiner who has additional responsibilities, devote their entire time to loan and trust companies under the Act and in particular to their supervision and examination. In addition to their review of the Registrar's memorandum and the discussions with the Registrar and members of his staff, the Committee interviewed during its New York hearings representatives, including examiners, of the Federal Reserve Bank of New York and the New York State Banking Department. These representatives outlined present-day procedures and policies of trust department examination in New York State and drew attention to the fact that increasing emphasis is now being placed upon examinations relating to a company's practices, policies and procedures, as opposed to more limited examinations relating solely to a company's financial solvency. The Committee was impressed by the knowledge and expertise displayed by these representatives. While there are obvious differences between the two jurisdictions, both in terms of size of the financial market and in terms of the structure and size of the financial institutions involved, the Committee does consider that the relatively recent emergence in the United States of trust department examination as a distinct and specialized type of bank examination should be noted and should serve to underline the continued importance of loan and trust examination in Ontario.

17.06 Section 126 (1) and (2) of the Act provides that:

> "126. (1) The Registrar personally shall visit or cause a duly qualified member of his staff to visit at least once annually the head office of each registered corporation, other than a corporation as to which he adopts the inspection of another government, and he shall inspect and examine the statements of the condition and affairs of

each corporation and make such inquiries as are necessary to ascertain its condition and ability to provide for the payment of its liabilities as and when they become due, and whether or not it has complied with this Act, and the Registrar shall report thereon to the Minister as to all matters requiring his attention and decision.

(2) Where the Registrar considers it necessary and expedient to make a further examination into the affairs of a corporation and so reports to the Minister, the Minister may in his discretion instruct the Registrar to visit or cause a duly qualified member of his staff to visit any branch office or offices of the corporation to inspect and examine into its affairs and to make such further inquiries as the Minister may require."

The Committee was advised that it is currently the policy of the Registrar to examine each Ontario corporation annually by visiting its head office and one or more branch offices in Ontario. If the Registrar considers it necessary to make a further examination of any branch office of an Ontario corporation outside Ontario, the prior approval of the Minister or his deputy is obtained under section 126 (2). The out-of-pocket disbursements of the examiners in making such an examination outside Ontario are charged to the corporation concerned under section 126 (6). The Registrar does not normally examine registered corporations incorporated under the Federal Acts or under the laws of another province on an annual basis but, with regard to these corporations, he adopts the inspection of the federal or other provincial authorities, as he is permitted to do by section 126 (1). Periodic visits are made to an Ontario office of these corporations to examine their operations and to discuss any matters which may have arisen, but these visits do not constitute full-scale examinations. Should the Registrar consider it necessary to visit a head office or branch office outside Ontario, authorization is obtained from the Minister or his deputy and the out-of-pocket expenses are charged to the corporation concerned. The Committee agrees with the principle stated in section 126 (1) that the Registrar should have a discretion as to the adoption of the inspection by another government. In the Committee's opinion, each corporation registered in Ontario should be given an annual examination, either by the Registrar and his staff, or, at the Registrar's discretion, by the examination staff of another government. If the Registrar is not satisfied with the examinations conducted by another government, then he should, in the Committee's opinion, conduct his own annual examination. The Committee understands that at present the exchange of information on examination procedures and results between the federal and provincial governments and between provincial governments themselves is not as extensive as it perhaps should be. Since

such an exchange has a bearing upon the exercise by the Registrar of his discretion under section 126 (1), the Committee recommends that the Government of Ontario assist the Registrar and his staff in promoting the adoption of common examination standards for loan and trust companies throughout Canada and the exchange of information between the regulatory authorities. With respect to examination staff, the Committee considers that it is a matter for the Registrar to determine the size of staff required in order to discharge the responsibilities imposed upon him by the Act and the legislation relating to deposit insurance. The Committee does wish to record its conclusion, however, that should the Registrar deem it necessary to add additional examination staff, any request therefor should receive immediate and appropriate action by the Government.

17.07 The Committee considers that a number of amendments should be made to section 126 to bring it up to date and to make it consistent with the practices being followed. The purposes of an examination as described in section 126 (1) should be broadened to include inquiries as to the policies of management; the Minister's approval for any examination at an office outside Ontario should no longer be required; the reference to the Registrar's "adoption" of the inspection of another government should be changed to refer to his being "satisfied" as to the inspection by another government; and the out-of-pocket disbursements of the examination staff for making an out-of-the-Province examination at a head office or any branch office of a registered corporation should be chargeable to the corporation concerned. The Committee therefore recommends that section 126 (1) of the Act be amended as follows:

> "126 (1) The Registrar personally shall visit or cause a duly qualified member of his staff to visit at least once annually the head office, or, if the Registrar considers it necessary, any branch office of each registered corporation, other than a corporation as to which he is satisfied as to the inspection of another government, and he shall inspect and examine the statements of the condition and affairs of each corporation and make such inquiries as are necessary to ascertain
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> (i) its financial condition;
>
> (ii) its ability to provide for payment of its liabilities as and when they become due;
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> (iii) the policies of its management; and
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> (iv) whether or not it has complied with this Act,
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> and the Registrar shall report thereon to the Minister as to all matters requiring his attention and decision."

It follows from the foregoing recommendation that section 126 (2) should

be repealed, the subsequent subsections renumbered, and subsection (6) amended to provide that where an examination is made of any head office or branch office situated outside Ontario, the corporation shall pay the account in connection with the examination upon the certificate of the Registrar.

17.08 The Committee understands that the annual fees for registration in Ontario are lower than the fees payable to other jurisdictions. For example, federal loan and trust companies pay substantially higher annual fees to the federal government due to the fact that the expenditures incurred for administering the Federal Acts are prorated annually among the companies licensed under those Acts.[12] While the Committee does not recommend adoption of the federal approach for Ontario, the Committee does consider that the fee scale currently in force should be reviewed.

17.09 **The Committee recommends that:**

(a) section 145 of the Act be amended so as to refer expressly to the Government of Ontario and the Minister as well as to the Registrar;

(b) a section be added to the Act providing that neither the Registrar, the Assistant Registrar nor any examiner shall be interested as a shareholder directly or indirectly in any registered corporation;

(c) sections 123 and 124 of the Act be amended to provide a sanction in the event that an examination made under either section should reveal that the assets of a corporation are insufficient to justify its continuance in business;

(d) sections 123 (1) and 126 (3) of the Act be amended so as to provide that the Registrar may inspect any books or records in the possession of the corporation;

(e) each registered corporation be examined no less frequently than annually, such examination to be made by the Registrar or, at his discretion, by the examination staff of another government, subject to the proviso that if the Registrar is not satisfied with respect to the examination performed on behalf of another government, the Registrar shall make his own examination;

(f) the Government of Ontario should assist the Registrar and his staff in promoting the adoption of common examination standards for loan and trust corporations throughout Canada and the exchange of information between regulators in the different jurisdictions;

(g) the Government of Ontario should act favourably and promptly in regard to any request received from the Registrar for additional examination staff;

(h) section 126 of the Act be amended so as to provide:

(i) that the Minister's approval shall not be required should the Registrar deem it necessary to examine any office of a registered corporation outside Ontario;

(ii) for inquiries as to the policies of the management of a registered corporation;

(iii) that the Registrar need only be satisfied as to the inspection carried out by another government; and

(iv) that a registered corporation shall pay any out-of-pocket expenses incurred by the Registrar or his staff in examining any office of the corporation outside Ontario; and

(i) the annual fees for registration in Ontario be reviewed.

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1. The Act, sections 166 and 167.
2. The Act, sections 123 and 124.
3. The Loan and Trust Corporations Amendment Act, 1970 (No. 2), S.O. 1970, c. 129, section 37. The provisions of section 37 are now found in sections 129 to 132 of the Act.
4. The Ontario Deposit Insurance Corporation Act, R.S.O. 1970, c. 307, section 23 (1).
5. Canada Deposit Insurance Corporation Act, R.S.C. 1970, c. C-3, section 13 (1).
6. Canada Deposit Insurance Corporation Act, R.S.C. 1970, c. C-3, sections 21 and 22.
7. Canada Deposit Insurance Corporation Act, R.S.C. 1970, c. C-3, section 23. In conducting his examination, the Registrar may exercise any of the powers given to him by subsections (3), (4) and (5) of section 126 of The Loan and Trust Corporations Act. See The Ontario Deposit Insurance Corporation Act, R.S.O. 1970, c. 307, section 31 (2) and (3).
8. Canada Deposit Insurance Corporation Act, R.S.C. 1970, c. C-3, section 29 (1).
9. It should perhaps also be mentioned that The Ontario Deposit Insurance Corporation Act, R.S.O. 1970, c.307 provides that the Registrar shall examine member institutions of the Ontario Deposit Insurance Corporation annually and report thereon to the Ontario Deposit Insurance Corporation. The Ontario Deposit Insurance Corporation is granted certain regulatory powers by that Act. Since deposit insurance policies are issued to loan and trust companies by CDIC only, these provisions are not operative at present.
10. The Insurance Act, R.S.O. 1970, c. 224.
11. The Insurance Act, R.S.O. 1970, c. 224.
12. The Department of Insurance Act, R.S.C. 1970, c. I-17, section 7.

CHAPTER 18

Auditors

18.01 The shareholders of Ontario corporations are required by the Act to appoint external auditors for the corporation annually under provisions that are basically the same as those contained in the BCA. Sections 72 and 73 of the Act, which apply to Ontario corporations only, provide for the appointment, removal and disqualification of the auditor and, with the amendments made to these sections in 1970,[1] adopt the same general approach to these matters as is to be found in sections 168, 169 and 170 of the BCA. Under the 1970 amendments, the vote of the shareholders required to remove any auditor before the expiration of his term of office was reduced from a two-thirds vote to a majority vote, and a number of BCA provisions were added to the Act with respect to: (i) prior notice by the corporation to the incumbent auditor of the intention to call a general meeting of shareholders for the purpose of passing a resolution removing him from office; (ii) notice to the incumbent auditor of the intention to nominate a new auditor for election at the annual meeting; and (iii) "related persons". Sections 72 and 73 were reviewed by the Committee and it did not appear that any major changes were required. The review did, however, raise several questions for consideration by the Committee as well as some deficiencies in the drafting of certain subsections of these two sections. These matters are discussed in the following paragraphs.

18.02 Section 72 (2) of the Act provides for the annual appointment of the auditors of an Ontario corporation by the shareholders, and section 72 (8) of the Act provides that, if for any reason no auditor is appointed, the Registrar may appoint the auditor and fix his remuneration. While no amendments to these provisions appeared necessary, the Committee observed that the Act, unlike the BCA, contains an express requirement with respect to the qualification of the auditor. Section 73 (2) states that "an auditor of a registered corporation shall be an accountant", and "accountant" is defined in section 1 of the Act as follows:

> "(a) 'accountant' means a person who is a member of The Canadian Institute of Chartered Accountants or any other person who is an accountant and who in either case, is acceptable to the Registrar as being competent to audit the accounts and transactions of corporations under this Act and includes a partnership of which the members are accountants;"

The Committee was of the view that, having regard to the importance of

loan and trust corporations as financial institutions, membership in The Canadian Institute of Chartered Accountants should be a mandatory requirement for any person appointed as the auditor of an Ontario loan or trust corporation. The Committee therefore recommends that the definition be changed by deleting the phrase "or any other person who is an accountant". The Committee was advised that in the case of Ontario corporations, the auditors are members of the Institute without exception. Consequently, it did not appear necessary to provide for an exception to the membership requirement. The Committee also noted that under the definition, the person appointed as auditor must be "acceptable to the Registrar". Although it seems unlikely to the Committee that the Registrar would, in exercise of this discretionary power, not accept the appointment of a member of the Institute in a particular case, and therefore the need to retain this discretion would seem doubtful, the Committee nevertheless favours its retention as a further safeguard. The Committee recommends, however, that the phrase "as being competent to audit the accounts and transactions of corporations under this Act" be deleted from the definition. The Committee intends that the new definition of accountant should apply elsewhere in the Act where the defined term is used, as for example in section 123 (3) under which the Registrar is given power to appoint an accountant to make a special audit of a corporation that is in default in filing its returns.

18.03 Under section 72 (9) of the Act, the corporation is required to give written notice to the auditor of his appointment forthwith after the appointment. Where an auditor is simply reappointed at an annual meeting, no valid purpose would seem to be served by requiring the corporation to give written notice to him of his reappointment, and, in fact, the section is more likely to be observed in the breach. The Committee recommends therefore that section 72 (9) be amended so that notice need only be given to an auditor at the time of his original appointment. A copy of the notice should at the same time be sent by the corporation to the Registrar. The Committee also recommends that a provision be inserted in the Act whereby a retiring auditor should be required to give written notice to the Registrar of his retirement.

18.04 The Committee reviewed subsections (10) and (11) of section 72, which were added to the Act in 1970, and which relate to the nomination of a person for auditor, other than the incumbent auditor. Subsection (10) provides that:

> "(10) A person, other than an incumbent auditor, may not be appointed auditor at an annual meeting unless notice of an intention to nominate that person to the office of auditor has been given by a shareholder to the corporation not less than fifteen days before

the meeting at which the auditor is to be appointed and where such notice is given the corporation shall send a copy of the notice to the incumbent auditor and to the person whom it is intended to nominate and shall give notice thereof to the shareholders in the manner specified in section 19."

The subsection precludes a shareholder from nominating at the annual meeting a person for appointment as auditor unless he has given the required 15 days' notice. Section 169 (1) of the BCA, with which it is comparable, does not contain this restriction and is based instead on the more real assumption that management, as the representative of the majority shareholders, is the most likely source of a desire to propose a new auditor for election at the annual meeting. Section 169 (1) provides that if reference is made in the information circular to action proposed to be taken at an annual meeting of shareholders with respect to the appointment of an auditor other than the incumbent auditor, the corporation shall, 15 days or more before the mailing of the notice of the meeting, give to the incumbent auditor written notice of management's intention not to recommend his reappointment at the annual meeting, specifying therein the date on which the notice of the meeting is intended to be mailed. Section 169 (2) then goes on to provide that the incumbent auditor has the right to make to the corporation, three days or more before the mailing of the notice of meeting, representations in writing concerning the proposal not to reappoint him as auditor, and the corporation, at its expense, shall forward with the notice of the meeting, a copy of such representations to each shareholder entitled to receive notice of the meeting. The Committee is aware of no valid reason why these provisions of the BCA should not also apply to Ontario corporations and therefore recommends that subsections (10) and (11) of section 72 be amended so as to adopt the approach followed by the BCA. It follows that if this recommendation is adopted, a shareholder will no longer be required to give prior notice to the corporation should he wish to nominate for election as auditor at the annual meeting a qualified person other than the incumbent auditor. If the subsections are amended as recommended, it will not be necessary to make amendments that would otherwise be required due to the Committee's earlier recommendations in paragraph 16.04 for lengthening the minimum notice required for a shareholders' meeting to 21 days.

18.05 The Committee noted in its review of section 73 of the Act that, although section 73 (1) added a definition of "related person" to the Act, the defined term is not used in section 73 (3) which is the operative section of the Act disqualifying certain persons from being appointed the auditor of a registered corporation. On comparison with

sections 170 (1) and 170 (2) of the BCA, it was noted that those sections used the defined term and they seemed to the Committee to present a clearer statement of the principles under which a person should be disqualified from being an auditor. The Committee observed that section 170 (2) prohibits a person appointed or acting as auditor from owning any "securities" of the corporation whereas section 73 (3) of the Act prohibits such a person from being a "shareholder" of the corporation. The Committee does not consider that it is necessary to extend the existing prohibition to include ownership by the auditor of a debt security of a registered corporation such as a debenture or a guaranteed investment certificate. Accordingly, the Committee recommends that section 73 (3) of the Act be replaced by the following two subsections:

> "No person shall be appointed auditor of a registered corporation who is a director, officer or employee of such corporation, or of any company in which such corporation has invested its funds under section 152 or 155, or who is a partner, employer or employee of any such director, officer or employee or who is a related person to any director, officer or employee of the corporation or of any such company.
>
> No person shall be appointed auditor of a registered corporation if he or any partner or employer of or related person to him beneficially owns, directly or indirectly, any shares of the corporation or of any company in which such corporation has invested its funds under section 152 or 155 or, if the corporation is a subsidiary of a holding corporation, any shares of its holding corporation."

18.06 Section 73 (3) of the Act prohibits the auditor from being a shareholder, director, officer or employee "of any company in which such [registered] corporation has invested its funds under section 152 or 155". The Committee received a submission requesting a change in this section that would prevent the auditor from being technically disqualified in a situation where he held a few shares in a "subsidiary" company and was unaware that the registered corporation had invested some of its funds in the shares of the same company. It was argued that the auditor should be permitted to dispose of his shares within a stated period after he first learns of the corporation's investment. The Committee was convinced by this submission and recommends that a divestiture provision be added to section 73 whereby the auditor may continue in that capacity so long as he disposes of his shares in the subsidiary company within six months of first learning of the registered corporation's investment.

18.07 A number of minor drafting changes would appear to be required in section 73. Subsection (6) can presumably be dropped now that

the two year period referred to has elapsed; the reference to "securities" in subsection (5) should be changed to "shares"; a definition of "holding company" should be added to the Act in view of the use of that term in subsection (5); and subsections (7) and (8) should be amended to correspond to subsections (5) and (6) of section 170 of the BCA which, in the case of the former subsection, prohibits a person from being appointed a receiver and manager or liquidator of a corporation if he "or any partner or employer of", or a related person to, him is or has been the auditor of the corporation; and, in the case of the latter subsection, prohibits a person who is appointed trustee in bankruptcy of a corporation or "any partner or employer of", or a related person to, him from being appointed to act as auditor of the corporation.

18.08 **The Committee recommends that:**

(a) no person shall be qualified to be appointed the auditor of a registered corporation unless such person is a member of The Canadian Institute of Chartered Accountants and is acceptable to the Registrar;

(b) a registered corporation should be required to give written notice to the auditor of his appointment at the time of his original appointment only and a copy of such notice should be given by the corporation to the Registrar;

(c) any auditor of a registered corporation who retires as auditor should be required to give written notice to the Registrar of his retirement;

(d) section 72 (10) and (11) of the Act be amended so as to follow the approach adopted in section 169 (1) and (2) of the BCA;

(e) section 73 (3) of the Act which relates to the disqualification of the auditor be replaced by two new subsections based on the principles contained in sections 170 (1) and (2) of the BCA, provided that there should be no prohibition against the auditor of a registered corporation owning a debt security of such corporation such as a debenture or guaranteed investment certificate;

(f) the Act should contain provision whereby the auditor of a registered corporation may dispose of any shares that he owns in a company in which the registered corporation may have invested its own funds pursuant to sections 152 or 155 of the Act, such disposal to be effected within a period of six months from the date that the auditor first learns of the investment by the registered corporation; and

(g) several amendments of a technical nature should be made to section 73.

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1. The Loan and Trust Corporations Amendment Act, 1970 (No. 2), S.O. 1970, c. 129, section 15.

CHAPTER 19

Financial Statements

19.01 A submission was received from The Institute of Chartered Accountants of Ontario (hereinafter referred to as the "Institute") recommending certain changes in sections 74 and 75 of the Act and in regulation 38/72 relating to the financial statements. These two sections apply to registered Ontario corporations only.[1] As indicated in the submission, the purpose of these recommendations was to bring the Act into closer accord with the BCA, the practices adopted by most companies, and generally accepted accounting principles. Section 74 (2) of the Act provides that "the auditor of a registered corporation shall make reports (a) to the shareholders on the financial statement of the corporation referred to in sections 19 and 75; and (b) to the Registrar on the annual statement filed with the Registrar under section 168". Section 74 (3) provides that:

> "In the reports required by subsection 2, the auditor shall state,
>
> (a) whether he has obtained all the information and explanations he has required;
>
> (b) whether in the opinion of the auditor the financial statement presents fairly the financial position of the corporation as at the date of the balance sheet included therein and the results of the operations of the corporation for the financial period ended on that date; and
>
> (c) whether the financial statements are in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding period, if any,
>
> in accordance with the information he has obtained and the explanations given to him and as shown by the books of the corporation."

Two submissions were made to the Committee with regard to the foregoing provisions. The first was that the form of the auditor's report to the shareholders of a registered corporation should be changed so as to conform with the form now required by section 171 (2) of the BCA in the case of a business corporation. This submission was accepted by the Committee. The second submission was that the form of report by the auditors on the annual statement (hereinafter referred to as the "Annual Statement") filed under section 168 of the Act should not be the same as the report to the shareholders on the financial statement under section 75. The Committee was advised that

the financial information presented in the financial statement and in the Annual Statement of a registered corporation is not the same; the former is usually prepared on a consolidated basis, while the latter is not; and the latter contains, in addition to the unconsolidated financial statements, some 32 pages of exhibits showing asset and liability breakdowns and other financial details, and a further ten pages of general information concerning the registered corporation. The Act currently requires the auditors to report on the entire Annual Statement including this detailed information. It was argued in the Institute's submission that the current format of the Annual Statement that is filed with the Registrar presents difficulties to the auditor since he is required to report that two quite different statements, one to shareholders and one to the Registrar, both present fairly the financial position of the corporation and the results of its operations. The Committee also heard representations from those responsible for the administration of the Act who favoured retention of the statutory obligation of the auditor to report on the entire Annual Statement. Concern was expressed that if the recommended change is made, the regulators would need some statutory power to obtain information from the auditors or to examine their working papers. The submission of the Institute appeared to the Committee to point up the practical problem of the auditor not being able to certify the entire Annual Statement without expanding the scope of their annual audit to a considerable degree at a substantial additional cost to each registered corporation. The Committee understands that the practice has been for auditors to submit to the Registrar reports that express denials of opinion as to certain supporting schedules forming part of the Annual Statement. The Committee also noted that section 168 (4) of the Act provides that the Annual Statement shall be proved by the affidavit of the president or vice-president and of the managing director, or some other principal officer of the corporation, and shall be accompanied by a certified copy of a resolution of the directors showing that such Annual Statement was adopted by them. This provision serves to indicate the importance that the Act attaches to correctness of the Annual Statement so far as the principal officers and directors of the registered corporation are concerned. For these reasons, the Committee accepts the Institute's submission and recommends that section 74 (1), (2) and (3) of the Act be replaced by the following new provisions:

"74 (1) The auditor shall make such examination as will enable him to make the reports required under subsections 2 and 3.

(2) The auditor shall make a report to the shareholders on the financial statement, other than the part thereof that relates to the period referred to in sub-clause ii of clause a of subsection 1 of section 75, to be laid before the shareholders at any annual

meeting during his term of office and shall state in his report whether in his opinion the financial statement referred to therein presents fairly the financial position of the corporation and the results of its operations for the period under review in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding period, if any.

(3) The auditor shall make a report to the Registrar on Part 1 of the annual statement filed with the Registrar under section 168 and shall state in his report whether:

(a) the special purpose financial statements contained in Part 1 are drawn up to show the financial position of the corporation and the results of its operations for the period under review in accordance with accounting practices prescribed or permitted by the Registrar applied on a basis consistent with that of the preceding period, if any; and

(b) the schedules contained in Part 1 set out all adjustments necessary for the reconciliation of such special purpose financial statements with those prepared for submission to the shareholders under section 75 (1)."

The Committee also recommends that section 168 (1) of the Act be amended so as to provide that the Annual Statement will consist of two parts, namely Parts 1 and 2; Part 1 to comprise the special purpose financial statements and schedules referred to in proposed new section 74 (3) (a) and (b) as recommended above, and Part 2 to comprise such further financial details and information as the Registrar may require. The Act should also provide that such special purpose financial statements shall consist of a statement of income, a statement of surplus, a statement of general reserve and a balance sheet, and that such statements shall be prepared in the form to be prescribed by the Registrar. The Committee understands that co-operation exists at the present time between the Registrar and the external auditors of registered corporations. A major reason for the co-operation is to eliminate duplication of effort between the auditors' audit staff and the Registrar's examiners. The Committee would expect this co-operation to continue notwithstanding these recommended changes and therefore does not consider that the Act should confer any new statutory right on the Registrar to obtain information from or to examine papers in the possession of the auditor. It follows from these recommendations that certain consequential amendments should be made to section 74. Subsection (4) should be amended so as to refer to "subsections 2 and 3". A new paragraph (d) should be added to section 74 (7) requiring the auditor in his reports to make such statements as he considers necessary "if he has not received all the

information and explanations that he has required". Paragraphs (a) and (b) of subsection (7) should be amended by adding the phrase "Part 1 of the" immediately before "annual statement". Finally, for greater certainty, the Committee recommends that, following the approach of the BCA, the term "financial statement" should be defined in section 1 of the Act to mean a financial statement referred to in section 75.

19.02 Section 75 (1) (a) of the Act describes the statements which make up the financial statement which the directors are required to lay before each annual meeting of shareholders. The Institute's submission pointed out that the wording of the section did not parallel that of section 172 (1) of the BCA and it was suggested that there was no reason for the wording to differ, except of course for differences in the designation of the statements comprising the financial statement. It was also submitted that with the adoption generally by registered corporations of the recommendations in The Canadian Institute of Chartered Accountants research study entitled "Accounting for Trust and Loan Companies",[2] there was no longer any need for a separate statement of accumulated reserves for investments as is now required by the Act. The Committee accepts these submissions and recommends that section 75 (1) of the Act be replaced with the following:

"The directors shall lay before each annual meeting of shareholders,

(a) a comparative financial statement relating separately to

(i) the period that commenced on the date of incorporation and ended not more than six months before the annual meeting or, if the corporation has completed a financial year, that commenced immediately after the end of the last completed financial year and ended not more than six months before the annual meeting, as the case may be, and

(ii) the period covered by the financial year next preceding such latest completed financial year, if any,

made up of:

(iii) a statement of income for each period,

(iv) a statement of surplus and, where ascertainable, showing severally a statement of contributed surplus and a statement of retained earnings for each period,

(v) a statement of general reserve for each period,

(vi) a balance sheet as at the end of each period;

(b) the report of the auditor to the shareholders;

(c) such further information respecting the financial position of

the corporation, as its letters patent, supplementary letters patent, or by-laws require."

It follows from the above that if this recommendation is adopted, it will be mandatory for registered corporations to present their figures in comparative form and the Registrar will no longer have a discretion in this respect as he now has under section 75 (1) (a). The Committee understands that most registered corporations are currently supplying information in their financial statement in comparative form, so the recommendation should not result in a change to a significant degree in the existing practice.

19.03 Since some registered corporations may not refer to the statements in their financial statement using the exact designations provided for in the Act, the Institute made a further submission to the Committee requesting adoption of a new subsection to section 75 giving recognition to such a practice. The Committee notes that a provision to this effect is found in section 172 (2) of the BCA. The Committee therefore recommends that a new subsection be added to section 75 as follows:

"It is not necessary to designate the statements referred to in subsection 1 as the statement of income, statement of surplus, statement of general reserve and balance sheet."

19.04 The Committee considered the general question whether a registered corporation should be required to include a statement of change in financial position (also known as a "statement of source and application of funds") in its financial statement. The discussions before the Committee with representatives of the Institute, in which representatives of the Registrar participated, led the Committee to conclude that such a statement would not be a meaningful statement for a loan company or a trust company. Accordingly, the Committee recommends that they not be required to furnish such a statement.

19.05 The Committee discussed certain of the provisions in regulation 38/72 which deals with financial statements. It was noted that the regulation contains certain defined terms in section 1 and it appeared to the Committee that some of these terms were also used in the Act.[3] The Committee recommends that any terms defined in the regulation which are also used in the Act should also be defined in section 1 of the Act. Two suggested changes in regulation 38/72 were received from the Institute. The first relates to section 6 of the regulation which deals with the disclosure required in a corporation's financial statement. With respect to paragraphs (h) and (i) of that section, it was pointed out that some uncertainty exists under the present wording which distinguishes between "loans on collateral securities" and "consumer loans". Since

some consumer loans are secured by collateral and others are not, confusion exists as to which of these two paragraphs applies. The Committee accepts and recommends adoption of the suggested revised wording of:

"(h) loans, secured;

(i) loans, unsecured;"

The second suggestion concerned section 2 (l) (r), (s) and (t) of the regulation which specifies a sequence of reporting income that is not followed by most trust companies today. The Committee accepts the Institute's submissions in this respect and recommends the adoption of the following sequence for Ontario corporations which is identical to the new wording suggested by the Institute:

"(q) the income or loss for the period before items (r), (t) and (v) inclusive;

(r) taxes on income applicable to the income or loss shown in item (q);

(s) the income or loss for the period before items (t) and (v);

(t) profits and losses on investments less applicable income taxes, if any;

(u) the net income or loss for the period before item (v);

(v) extraordinary items, less applicable income taxes, if any;

(w) the net income or loss for the period."

19.06 **The Committee recommends that:**

(a) the form of the auditor's report to the shareholders should be changed so as to follow the wording required under the BCA;

(b) the auditor should be required to report to the Registrar on Part 1 of a registered corporation's Annual Statement only, that is the portion of the statement containing the financial statements and supporting schedules reconciling these statements with the financial statement to the shareholders;

(c) no new section be added to the Act conferring on the Registrar a statutory right to obtain information from the auditor or to examine the auditor's working papers;

(d) section 74 (7) of the Act should be amended (a) by adding thereto a new paragraph requiring the auditor in his reports to make such statements as he considers necessary "if he has not received all information and explanations that he has required"; and (b) the reference to the Annual Statement in paragraphs (a) and (b) should be changed so as to constitute a reference to Part 1 of the Annual Statement only;

(e) the term "financial statement" should be defined in section 1 of the Act to mean a financial statement referred to in section 75;

(f) registered corporations should be required to prepare the financial statement under section 75 (1) in comparative form;

(g) section 75 (1) (a) of the Act should be amended so as to follow the wording of section 172 (1) of the BCA;

(h) a new subsection be added to section 75 providing that registered corporations not be required to designate the statements referred to in subsection (1) of section 75 as the statement of income, statement of surplus, statement of general reserve and balance sheet;

(i) registered corporations not be required to include in their financial statement a statement of change in financial position;

(j) defined terms in section 1 of regulation 38/72 should also be defined in section 1 of the Act, to the extent that such terms are used in various sections of the Act; and

(k) section 2 (1) (q) to (w) of regulation 38/72 and section 6 (1) (h) and (i) of the same regulation be amended as recommended in paragraph 19.05 above.

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1. The Act, section 2 (3).
2. Accounting for Trust and Loan Companies in Canada, a Research Study, The Canadian Institute of Chartered Accountants, Toronto, September, 1971.
3. See, for example, section 73 (5) of the Act which uses the term "holding company" and section 74 (7a) of the Act which refers to "subsidiary". These terms are not defined in the Act but are defined in regulation 38/72.

APPENDIX

Proposed New Section Stating Objects Of Trust Companies

84. (1) Subject to sections 87, 88 and 89 and to any provisions of this Act respecting the investment of moneys received for guaranteed investment or as deposits, a provincial trust company may and any other registered trust company that has capacity to do so may:

(a) take, receive and hold all estates and real and personal property that may be granted, committed, transferred or conveyed to the company with its consent, upon any trust or trusts whatsoever not contrary to law, at any time or times, by any person or persons, body or bodies corporate, or by any court of competent jurisdiction;

(b) take and receive as trustee or a bailee, upon such terms and for such remuneration as are agreed upon, deeds, wills, policies of insurance, bonds, debentures or other valuable papers or securities for money, jewelry, plate or other chattel property of any kind, and to guarantee the safe keeping of the same;

(c) receive and store for safe keeping all kinds of securities and personal property and rent spaces or compartments for the storage of securities or personal property and enter into contracts for regulating the terms and conditions upon which such business is to be carried on;

(d) act generally as attorney or agent for the transaction of business, the sale or purchase of any real or personal property, the winding up of estates and partnerships, the receipt or collection of loans, rents, interest, dividends, debts, mortgages, debentures, bonds, bills, notes, coupons and other securities for money;

(e) act as investing and managing agent of estates, properties and trusts for and on behalf of executors, administrators and trustees or other persons;

(f) act as transfer agent, registrar, authenticating agent, disbursing agent or fiscal agent for any person, organization, association, trust, body corporate, municipality or government, and to receive, invest and manage any sinking fund on such terms as are agreed upon;

(g) accept and execute the offices of executor, administrator, trustee, indenture trustee, receiver, liquidator, assignee, bailee, custodian, trustee in bankruptcy, trustee for the benefit of creditors, guardian of any minor's estate, committee of any mentally incompetent person's estate, arbitrator, valuator or appraiser, and perform the duties of such offices or trusts as fully and completely as any person so appointed;

(h) invest any trust money in the hands of the company in any securities in which private trustees may by law invest trust money;

(i) charge, collect and receive all proper remuneration, legal, usual and customary costs, charges and expenses for all such services, duties and trusts.

(2) A provincial trust company and any other registered trust company that has the capacity to do so has power as incidental and ancillary to the objects set out in subsection (1) to,

(a) make, enter into, deliver, accept and receive all deeds, conveyances, assurances, transfers, assignments, grants and contracts necessary to carry out the purposes of the company, and promote its objects and business;

(b) take any mortgage or other security as may be deemed expedient for any moneys owing to the company and sell, pledge or mortgage any mortgage or other security, or any other real or personal property held by the company, and make and execute all requisite conveyances and assurances in respect thereof;

(c) draw, make, accept, endorse, discount, execute and issue bills of exchange, promissory notes, bills of lading, warrants and other negotiable or transferable instruments;

(d) adopt such means of making known the services of the company as may seem expedient, and in particular by advertising, by purchase and exhibition of works of art or interest, by publication of books and periodicals and by granting prizes and rewards and making donations;

(e) cause the company to be registered and recognized in any foreign jurisdiction or any province or territory of Canada, and designate persons therein according to the laws of that foreign jurisdiction or that province or territory of Canada to represent the company and to accept service for and on behalf of the company of any process or suit;

(f) allot and issue fully-paid shares of the company in payment or part payment of any property purchased or otherwise acquired by the company which is an authorized investment under section 153 (1);

(g) establish agencies and branches;

(h) pay all costs and expenses of or incidental to the incorporation and organization of the company.